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TRANSCRIPT OF RECORD

Supreme Court of the United States

OCTOBER TERM, 1942

No. 429

HURLBUT W. SMITH, PETITIONER,

vs.

FRANK J. SHAUGHNESSY, COLLECTOR OF INTERNAL REVENUE OF THE UNITED STATES FOR THE TWENTY-FIRST DISTRICT OF NEW YORK

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITION FOR CERTIORARI FILED SEPTEMBER 29, 1942.

CERTIORARI GRANTED NOVEMBER 9, 1942.

SUPREME COURT OF THE UNITED STATES

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[fol.1]

IN UNITED STATES DISTRICT COURT, NORTHERN DISTRICT OF NEW YORK

Civil #386

HURLBUT W. SMITH, Plaintiff-Appellee,

vs.

FRANK J. SHAUGHNESSY, Collector of Internal Revenue for the Twenty-first District of New York, Defendant-Appellant.

STATEMENT UNDER RULE 13

The above entitled action for recovery of alleged erroneous United States gift taxes for 1937 paid by the plaintiff was commenced in the United States District Court for the Northern District of New York by filing of complaint with the Clerk of said Court March 14, 1940, and issuance and service of the summons and complaint on the defendant Collector March 14, 1940. Judgment for the plaintiff was entered September 10, 1941, in amount of $40,109.19 with interest from March 18, 1938, and costs of $24.60.

The above caption shows the names of the plaintiff and defendant. There have been no parties added and there [fol. 2] has been no change in the parties thereto or their attorneys, or on this appeal.

Mackenzie, Smith & Michell, Attorneys of Syracuse, N. Y., appeared and appear for the plaintiff-appellee, and Ralph L. Emmons, U. S. Attorney for the Northern District of New York of Binghamton, N. Y., for the defendant-appellant.

The dates of filing the respective pleadings are stated in the record.

The trial was held at Syracuse, N. Y., October 28, 1941, before Honorable Frederick H. Bryant, U. S. District Judge, without a jury, and a copy of his opinion is printed in full in the record. Stipulation of most of the pertinent facts is printed in the stenographer's minutes.

Appeal was taken by the defendant December 10, 1941.

IN DISTRICT COURT OF THE UNITED STATES, NORTHERN DISTRICT OF NEW YORK

[Title omitted]

COMPLAINT—Filed March 14, 1940

Comes the plaintiff above named, and for his cause of action against the defendant herein alleges:

[fol. 3] 1. That he is a citizen of the State of New York and of the United States, and a resident of the City of Syracuse, County of Onondaga and State of New York, and of the Northern District of New York, and brings this action, arising under the Internal Revenue Laws of the United States, against the defendant above namod to recover the sum of $71,674.22, with interest thereon, representing gift taxes illegally and erroneously assessed and exacted from plaintiff.

2. That at all the times herein mentioned the defendant, Frank J. Shaughnessy, was and now is a resident of the City of Syracuse, County of Onondaga and State of New York, and of the Northern District of New York, and was and now is the duly appointed, qualified and acting Collector of Internal Revenue of the United States for the Twenty-first District of New York.

3. Plaintiff further alleges that on the 26th day of February, 1937, pursuant to the provisions, among others, of a certain Trust Indenture dated on that day, executed by and between the said plaintiff and The Syracuse Trust Company, a banking corporation of Syracuse, New York, the plaintiff assigned, transferred and set over irrevocably unto said The Syracuse Trust Company and its successors three thousand (3,000) shares of the convertible preferred stock of L. C. Smith & Corona Typewriters, Inc., a New York corporation, having its principal office and place for the transaction of business in the City of Syracuse, New York, in trust nevertheless, to manage and control said property and to keep the same or the proceeds thereof invested, and to collect the income thereof and to pay over the net income from said trust fund quarterly to and for the use of Gladys D. Smith, wife of the plaintiff, during [fol. 4] her life, and upon her death, to pay over the principal of said trust fund to the plaintiff, if he be then living, or

in the event of the death of the plaintiff, prior to the death of his said wife, to pay over said principal of said trust to such person or persons and in such amounts and proportions as the said life beneficiary should by her last will and testament direct, and in the event of her failure to make testamentary disposition thereof, then to such person or persons and in such amounts and proportions as would take the same under the Laws of the State of New York in case the principal of said trust fund had been owned outright by the said life beneficiary and she had died intestate.

4. That thereafter, upon a return of said transaction made and filed with the defendant by plaintiff on or about March 15, 1938, the said defendant, Collector for the Twenty-first District of New York, assessed a Federal Gift Tax thereon in the amount of $71,674.22, which tax was paid by plaintiff to the defendant Collector as aforesaid, on March 15, 1938.

5. That thereafter, and on or about March 18, 1938, the plaintiff filed with said defendant, Collector as aforesaid a duly verified claim, in form as approved by law, for the refund of said tax so assessed, collected and paid, on the ground that the transfer set forth in said Trust Indenture did not constitute a taxable gift. True copies of said claim and of the said Trust Indenture thereto annexed, are hereto attached, Marked "Schedule A" and are hereby referred to and made a part of this complaint.

6. That thereafter, and on or about April 15, 1938, the Commissioner of Internal Revenue rejected said claim for refund in its entirety and, on said date, as plaintiff is informed and believes, sent to plaintiff by registered mail [fol. 5] a copy of his letter of rejection dated on said date, which letter was received by plaintiff on or about April 16, 1938, said letter stating in part as follows:

"Your claim is based upon the contention that the value of the trust estate created by the trust agreement of February 26, 1937, for the benefit of your wife, does not constitute a taxable gift.

Since it appears from the trust agreement that you have parted with all dominion and control over the trust estate and have no power to cause the beneficial title of the trust estate to be revested in yourself, the transfer is complete and taxable under the provisions of article 3 of the Regula-

tions 79 (1936 Edition) relating to the gift tax under the Revenue Act of 1932, as amended and supplemented by the Revenue Acts of 1934 and 1935.

Accordingly, your claim for refund is rejected in its entirety."

A true copy of said letter rejecting said claim for refund is hereto attached marked "Schedule B" and is hereby referred to and made a part of this complaint.

7. That as plaintiff is informed and believes, the transfer under said Trust Indenture did not and does not constitute a taxable gift under the Internal Revenue Laws of the United States, and that the aforesaid tax thereon was illegally and erroneously assessed and collected and that no part of said tax has been refunded or repaid.

Wherefore plaintiff demands judgment against the defendant for said sum of $71,674.22 with interest thereon [fol. 6] from March 15, 1938, together with the costs and disbursements of this action.

Mackenzie, Smith & Michell, Attorneys for Plaintiff, Office & Postoffice Address, 821 Onondaga County Savings Bank Building, Syracuse, New York.

William A. Mackenzie, Basil B. Aylesworth, Members of the firm of Mackenzie, Smith & Michell, and two of the attorneys of record for plaintiff.

Duly sworn to by Hurlbut W. Smith. Jurat omitted in printing.

[fol. 7] SCHEDULE "A"

Claim

To be filed with the Collector where assessment was made or tax paid

Collector's Stamp
(Date received)

The Collector will indicate in the block below the kind of claim filed, and fill in the certificate on the reverse side.

(V) Refund of tax illegally collected.
( ) Refund of amount paid for stamps unused, or used in error or excess.
( ) Abatement of tax assessed (not applicable to estate or income taxes).

STATE OF NEW YORK,
County of Onondaga, ss:

(Type or Print)

Name of taxpayer or purchaser of stamps, Hurlbut W. Smith.

Business address, 701 E. Washington St., Syracuse, New York.

Residence, 1111 James St., Syracuse, New York.

The deponent, being duly sworn according to law, deposes and says that this statement is made on behalf of the taxpayer named, and that the facts given below are true and complete:

1. District in which return (if any) was filed, 21st New York.

2. Period (if for income tax, make separate form for each taxable year) from Jan. 1, 1937, to Dec. 31, 1937.

[fol. 8] 3. Character of assessment or tax, Gift tax.

4. Amount of assessment, ~~$71~~,674.22; dates of payment, March 15, 1938.

5. Date stamps were purchased from the Government.

6. Amount to be refunded, $71,674.22.

7. Amount to be abated (not applicable to income or estate taxes) $——.

8. The time within which this claim may be legally filed expires, under Section 501-532 of the Revenue Act of 1932, March 15, 1941.

The deponent verily believes that this claim should be allowed for the following reasons:

(1) That the transfer set forth in the Trust Indenture upon which said tax was based (a true copy of which Indenture is hereto annexed and marked "Exhibit A") did not constitute a taxable gift;

(2) That in and by the terms of said Trust Indenture it is provided that upon the death of the life beneficiary, the Trustee shall pay over the principal of the trust fund to the Settlor, Hurlbut W. Smith, the claimant herein, if he is then living, and that said Trust Fund therefore does not constitute a taxable gift.

Signed Hurlbut W. Smith.

Sworn to and subscribed before me this 18th day of March, 1938. Henry A. Eiler, Notary Public. (Seal.)

[fol. 9] EXHIBIT "A" TO CLAIM

This Indenture, made, executed and delivered in the City of Syracuse, Onondaga County, New York, on the 26th day of February, 1937, by and between Hurlbut W. Smith, of said City (hereinafter called the "Settlor"), and The Syracuse Trust Company (hereinafter called the "Trustee", Witnesseth:

First—The Settlor hereby assigns, transfers and sets over irrevocably unto the Trustee and its successors all the following described property:

Three Thousand (3,000) shares of the Convertible Preferred Stock of L. C. Smith & Corona Typewriters, Inc.

To Have and To Hold unto the Trustee and its successors, in trust however for the uses and purposes following:

1. To care for, manage and control the said property (including any and all that may be hereafter assigned by the Settlor to the Trustee by written assignment therein expressly stated to be for the purposes set forth in this Indenture and subject to the terms and conditions hereof), to keep the same, or the proceeds thereof, invested, to collect the income thereof, and to pay over the net income from said trust fund quarterly to and for the use of Gladys D. Smith, wife of the Settlor, (hereinafter sometimes called the "Life Beneficiary"), during her life, and upon her death to pay over the principal of said trust fund to the Settlor, Hurlbut W. Smith, if he is then living, or in the event of the death of said Settlor prior to the death [fol. 10] of the said Life Beneficiary, to pay over said principal of said trust fund as follows:

The Trustee shall upon the death of the said Life Beneficiary pay over the principal of said trust to such person or persons and in such amounts and proportions as the said Life Beneficiary may by her last will and testament direct, and in the event of her failure to make testamentary disposition thereof, then and in that event the principal of the trust herein created for her life shall be paid over and delivered by the Trustee to such person or persons and in such amounts and proportions as would take the same under the laws of the State of New York in case the principal of said trust fund had been owned outright by the said Life Beneficiary and she had died intestate.

2. No assignment or order of the Life Beneficiary by way of anticipation of any part of the income of the trust herein created shall be valid, but the income shall be paid by the Trustee to the person entitled to receive it under the provisions hereof, or deposited to her account in some bank of good standing and repute, without regard to any assignment or order. Nor can the principal or income of said trust become attached by trustee process or garnishment or other legal proceeding while in the hands of the Trustee, except to the extent permitted by the laws of the State of New York.

3. The Trustee may receive any other property, real or personal, including life insurance policies, devised, bequeathed, assigned, granted or conveyed by the Settlor or by any other person for the purpose of the trust hereby created, and all such property shall be held by the Trustee subject to the terms of this Indenture in the same manner as if it had been included in the description of the property [fol. 11] hereby transferred to the Trustee. Any sums of money or other property so received shall immediately constitute a trust fund and be added to the principal of the trust created hereby, to be held, managed and invested, and payments therefrom made in accordance with the provisions hereof.

4. The Trustee shall have full power and authority to hold and retain any of the property coming into its hands hereunder, or that may hereafter become subject to the terms of this Indenture, in the same form of investment as that in which it is received by it, although it may not be of the character of investment permitted by law to trustees.

The Settlor reserves to himself during his lifetime, however, the power to direct the sale or retention of any such assets or of any other assets that may hereafter be purchased by the Trustee and become part of the principal of the trust created hereby, at such times and for such price as he may think wise, and the power to supervise the reinvestment of any moneys at any time in the hands of the Trustee, and the Trustee is is hereby relieved from any and all liability because of any such sale, retention or reinvestment if the same be authorized or directed by the Settlor by instrument in writing signed by him and filed with the Trustee. The Settlor also reserves to himself during his lifetime the power to require the Trustee to execute proxies to him or his nominee to vote any shares of stock at any time held by the Trustee as part of the principal of the trust created hereby, and the Trustee hereby agrees, upon request of the Settlor in writing signed by him and filed with the Trustee, to execute and deliver any such proxies.

5. In the event of the death of the Settlor prior to the termination of the trust created hereby the Trustee shall [fol. 12] thereafter have absolute authority, in its absolute and uncontrolled discretion, to sell, lease, mortgage or exchange the whole or any part of any property at any time constituting a part of the principal of the trust created hereby, upon such terms and conditions as may to it seem advisable, and to invest and reinvest any of the trust funds held hereunder as to it may seem proper, although the same may not be of the character of investment permitted by law to trustees.

6. Without intending to impose any legal obligation upon the Trustee or to restrict its action in the exercise of any discretionary powers granted to it hereby, the Settlor desires to express the wish that after his death the Trustee keep the Life Beneficiary of the trust hereby created fully advised as to the nature and condition of the trust property held by it for her life benefit and advise and confer with her from time to time regarding the investment and reinvestment of the principal of the trust held for her life benefit under the provisions of this Indenture.

7. If so directed by the Settlor during his lifetime by an instrument in writing duly signed by him and filed with the Trustee, and in its absolute and uncontrolled discretion

after the death of the Settlor and during the continuance of this trust, the Trustee shall have the right to exchange any of the stocks, bonds and/or other securities constituting the trust for the stocks, bonds and/or other securities of any corporation or corporations which may be a party to any reorganization for the purpose of conducting a business of the same kind or similar to or including that conducted by the company the stocks, bonds and/or other securities of which are so exchanged, whether such stocks, bonds and/or other securities be received in whole or in [fol. 13] part payment for the stocks, bonds and/or other securities exchanged.

8. The Trustee shall apply the entire income of all securities at any time held by it hereunder to the use of the Life Beneficiary irrespective of the price paid for them or their market value at any time, it being intended hereby that no part of such income shall be applied as a sinking fund to offset the gradual loss of the premium upon or market value of such securities. All taxable stock dividends, rights and capital gains shall be trated as principal so far as permitted by law, and any income tax that may become payable thereon shall be paid by the Trustee from the principal.

8. The Trustee shall annually render an account to the Life Beneficiary, and such account, when approved by such Life Beneficiary, shall be binding and final upon all parties, and, together with receipts for full payments in accordance therewith shall be a full acquittance and release to the Trustee without any further accounting in any court.

10. The Trustee may resign at any time on giving thirty days notice of such resignation, and upon such resignation becoming effective, or if the Trustee shall for any reason become incapable of performing its duties, the Settlor, if living, and in case of his prior death the Life Beneficiary of the trust, shall appoint a successor trustee by instrument in writing signed by him or her in duplicate, one of which duplicates shall be filed with the successor trustee and one with the Trustee named herein, whereupon the Trustee herein named shall forthwith account to such successor trustee, and such successor trustee shall thereafter have all of the powers and be subject to the same requirements [fol. 14] as those provided hereby with respect to the Trustee herein named.

11. The trust hereby created shall be deemed a New York trust, and shall in all respects be governed by the laws of the State of New York.

Second—The Trustee accepts said trust, and agrees to carry out the provisions hereof on its part.

In Witness Whereof, the Settlor has hereunto set his hand and seal, and the Trustee has caused these presents to be executed by its duly authorized officer and its corporate seal to be hereunto affixed, the day and year first above written.

Hurlbut W. Smith, (L. S.) The Syracuse Trust Company, by Harold C. Beatty, Trust Officer.

State of New York,
County of Onondaga, ss.:

On this 26 day of February, 1937, before me personally appeared Hurlbut W. Smith, to me known and known to me to be the same person named in and who executed the foregoing instrument, and he duly acknowledged to me that he executed the same.

Harriet M. Baldwin, Notary Public, Onondaga Co., N. Y.

[fol. 15] State of New York,
County of Onondaga, ss.:

On this 26 day of February, 1937, before me personally appeared Harold C. Beatty, to me known, who being duly sworn deposes and says that he resides at Skaneateles, N. Y., and is the Trust Officer of The Syracuse Trust Company, the corporation named in and which executed the foregoing instrument; that he knows the seal of said corporation; that the seal affixed to said instrument in such corporate seal, that it was so affixed thereto by order of the Board of Directors of said corporation, and that he signed his name thereto by like order.

Harriet M. Baldwin, Notary Public, Onondaga Co., N. Y.

Schedule "B"

Copy of Letter from Treasury Department—Washington

Office of Commissioner of Internal Revenue.

Address reply to Commissioner of Internal Revenue and Refer to MT-ET-GT-234-37-21st New York.

Donor—Hurlbut W. Smith. Apr. 15, 1938.
Mr. Hulbut W. Smith, 701 East Washington Street, Syracuse, New York.

[fol. 16] Sir:

Reference is made to your claim, Form 843, filed on March 15, 1938, for refund of Federal Gift Tax paid for the calendar year 1937 in the amount of $71,674.22.

Your claim is based upon the contention that the value of the trust fund created by the trust agreement of February 26, 1937, for the benefit of your wife, does not constitute a taxable gift.

Since it appears from the trust agreement that you have parted with all dominion and control over the trust estate and have no power to cause the beneficial title of the trust estate to be revested in yourself, the transfer is complete and is taxable under the provisions of article 3 of the Regulations 79 (1936 Edition) relating to the gift tax under the Revenue Act of 1932, as amended and supplemented by the Revenue Acts of 1934 and 1935.

Accordingly, your claim for refund is rejected in its entirety.

Respectfully, Guy T. Helvering, Commissioner, by
(Signed) D. S. Bliss, Deputy Commissioner.

[fol. 17] In District Court of the United States, Northern District of New York

[Title omitted]

Answer—Filed June 7, 1940

The defendant for answer to the complaint herein

1. Admits all the material allegations thereof except he denies the allegations in paragraph 1, that the action is for a sum of money "representing gift taxes illegally and erroneously assessed and exacted from the plaintiff," and denies the allegations contained in paragraph 7 that "the transfer under the said Trust Indenture did not and does not constitute a taxable gift under the Internal Revenue Laws of the United States, and that the aforesaid tax thereon was illegally and erroneously assessed and collected."

2. As an affirmative defense to any alleged personal liability of defendant, said defendant alleges that all his acts in respect to said tax and matters alleged in the complaint were performed pursuant to the provisions of law and to the official duties of his office as Collector of Internal Revenue of the United States for the 21st District of New [fol. 18] York, and under the directions of the United States Commissioner of Internal Revenue.

Wherefore, defendant demands that said complaint be dismissed with costs.

Ralph L. Emmons, United States Attorney and Attorney for Defendant, Office and Postoffice Address, Federal Building, Binghamton, N. Y.

IN UNITED STATES DISTRICT COURT, NORTHERN DISTRICT OF NEW YORK

[Title omitted]

Statement of Evidence

Minutes of Proceedings had in the above entitled Matter at a Regular Term of the United States District Court held in and for the Northern District of New York, Federal Building, Syracuse, New York, on Monday, October twenty-eighth (28), 1940, commencing at ten-thirty o'clock in the forenoon, Eastern Standard Time.

Presiding: Honorable Frederick H. Bryant, United States District Judge.

[fol. 19] Appearances:

Messrs. Mackenzie, Smith and Michell, Attorneys and Counselors at Law, Onondaga County Savings Bank Building, Syracuse, New York, (Willis H. Michell, Esquire, and Basil B. Aylesworth, Esquire, of Counsel, appearing) Solicitors for the Plaintiff.

Honorable Ralph L. Emmons, United States Attorney in and for the Northern District of New York, by

B. Fitch Tompkins, Esquire, Assistant United States Attorney; and

Julian G. Gibbs, Esquire, Special Assistant to the Attorney General, Washington, D. C., Solicitors for the Defendant.

Mr. Michell: May it please the Court: This is an action brought by Hurlbut W. Smith against Frank J. Shaughnessy, Collector of Internal Revenue of the United States for the Twenty-first District of New York to recover a gift tax paid by him on or about March 15, 1938.

On February 26, 1937 Mr. Smith executed a trust indenture to the Syracuse Trust Company, as Trustee, whereby he established a trust fund consisting of three thousand shares of the six per cent convertible preferred stock of the L. C. Smith and Corona Typewriters Inc. The trust indenture provided that the income from the trust fund should be paid to Gladys D. Smith for life, with the remainder upon her death to the Plaintiff, if living, and if not then living, to her legatees, or if she died intestate, to her distributees under the laws of the State of New York,

Now the trust indenture, as I have said, was executed on February 26, 1937. On March 15, 1938 Mr. Smith filed a [fol. 20] federal gift tax return of said transfer showing the value of the trust fund of five hundred seventy thousand nine hundred thirty-seven dollars fifty cents, and a net taxable gift of the entire fund after deduction of exemptions of five hundred twenty-five thousand nine hundred thirty-seven dollars and fifty cents, and he paid a gift tax thereon of seventy-one thousand six hundred seventy-four dollars twenty-two cents. Shortly thereafter he filed a claim for a refund of said gift tax and on April 15, 1938 the Commissioner rejected said claim in its entirety, and this action is brought to recover the proper amount of this gift tax.

It is the Plaintiff's contention that this tax should only be the value of her life estate in this trust fund, either upon the basis of four per cent, or upon a fixed and determined basis of six per cent on the three thousand shares, or eighteen thousand dollars.

The gift tax due on the first basis, less an exemption of forty-five thousand dollars, has been computed at thirty-one thousand five hundred sixty-five dollars and three cents; and on the second basis at the sum of twenty thousand two hundred sixty-one dollars thirty-three cents, and that we claim we should have the balance between those figures and the seventy-one thousand dollars which he actually paid, on either one or the other of those two theories.

I think I might say that the complaint alleges certain matters as facts, and the answer admits those statements.

For the convenience of Your Honor,—I think there will be no objection to this from Mr. Gibbs,—I would like to submit photostatic copies of certain papers mentioned in the complaint.

Mr. Gibbs: That is right. That is, the trust indenture? [fol. 21] Mr. Michell: Well the other papers are a check in payment of the tax and a letter of the Commissioner rejecting the claim.

Mr. Gibbs: No objection to the trust indenture.

The Court: You want it marked in evidence?

Mr. Michell: I think that probably we better.

The Court: All right. Received.

(Trust indenture dated February 26, 1937 between Hurlbut W. Smith and the Syracuse Trust Company received in evidence as Plaintiff's Exhibit Number 1 of this date.)

Mr. Michell: I offer in evidence Plaintiff's Exhibit 1, being an indenture made, executed and delivered in the City of Syracuse, Onondaga County, New York, on the 26th day of February, 1937, by and between Hurlbut W. Smith, designated as the settler, and the Syracuse Trust Company, designated as the Trustee.

The Court: Received.

Mr. Michell: I offer in evidence as Exhibit 2, the original gift tax return of Hurlbut W. Smith, subscribed and sworn to by him on the 15th day of March 1938, and the affidavit of the Notary thereto attached. This is the original return and bears the stamp: "Received, Filed March 21, 1938". With the permission of the Court I would like to offer this in evidence and to substitute a copy, because it is the original.

Mr. Gibbs: No objection.

The Court: All right. Received.

(Gift tax return of Hurlbut W. Smith sworn to March 15, 1938 received in evidence and marked Plaintiff's Exhibit Number 2 of this date.)

Mr. Michell: I offer in evidence as Exhibit 3 the check [fol. 22] dated March 15, 1938 drawn by H. W. Smith on the Syracuse Trust Company, payable to the Collector of Internal Revenue at Syracuse, New York, for seventy-one

thousand six hundred seventy-four dollars twenty-two cents. With the permission of the Court I would like to withdraw that at the same time and substitute a photostatic copy.

The Court: Received.

Mr. Gibbs: There is no objection, of course, Mr. Michell, as to the date of that check, but I do not believe that is the actual date of the payment of the tax. I think you have got the date noted on the Collector's record. If you are offering that for the purpose that in the event you should win the case and your refund dates back to a certain date as to payment of interest you must be careful as to the exact date.

Mr. Michell: Upon the back of this check, Exhibit 3 appears the following legend: "Received Payment through Syracuse Clearing House March 18, 1938, prior endorsement guaranteed. Merchants National Bank and Trust Company" by somebody "Assistant Cashier."

Mr. Gibbs: No objection.

The Court: Received.

(Photostatic copy of check dated March 15, 1938 payable to Collector of Internal Revenue, Syracuse, New York, in the amount of $71,674.22 by H. W. Smith received in evidence as Plaintiff's Exhibit Number 3 of this date.)

Mr. Michell: I offer in evidence as Exhibit 4 the claim filed by Hurlbut W. Smith, sworn to and subscribed on the 18th day of March, 1938 before Henry A. Eiler, Notary Public, in which he claims refund in the amount of seventy-one thousand six hundred seventy-four dollars twenty-two [fol. 23] cents, and inasmuch as this the original claim produced by the Government I would like to substitute a copy therefor.

Mr. Gibbs: No objection.

Mr. Michell: I think I might also say that the original bears the legend under the Collector's stamp; "Collector, twenty-first district, N. Y., March 15, 1938, Miscellaneous Tax, Division Internal Revenue."

The Court: Received.

(Claim filed by Hurlbut W. Smith sworn to March 18, 1938 for refund on $71,674.22 received in evidence as Plaintiff's Exhibit Number 4 of this date.)

Mr. Michell: Will you mark this please?

(Photostatic copy of letter dated April 15, 1938 to Hurlbut W. Smith from Guy T. Helvering, Commissioner, by D. S. Bliss, Deputy Commissioner, Treasury Department, Washington, marked Plaintiff's Exhibit Number 5 for identification of this date.)

(Exhibit shown to Mr. Gibbs by Mr. Mitchell.)

Mr. Gibbs: No objection to introducing Exhibit 5.

Mr. Michell: I offer in evidence Exhibit 5, a letter from the Treasury Department, Washington, addressed to Mr. Hurlbut W. Smith, 701 East Washington Street, Syracuse, New York, dated April 15, 1938, signed Guy T. Helvering, Commissioner, by D. S. Bliss, Deputy Commissioner, rejecting the claim for refund in its entirety.

Here again I would like to substitute a photostatic copy.

(Photostatic copy of letter dated April 15, 1938 to Hurlbut W. Smith from Guy T. Helvering, Commissioner, by D. S. Bliss, Deputy Commissioner, Treasury Department, [fol. 24] Washington, previously marked for identification, received in evidence as Plaintiff's Exhibit Number 5 of this date.)

Mr. Michell: This morning after Your Honor granted us the courtesy of a recess we agreed upon a stipulation, subject to objection however on the part of either party to the competency, revelancy or materiality of the stipulation itself. Is that a correct statement, Mr. Gibbs?

Mr. Gibbs: That is correct.

Mr. Michell: Now if you will watch me I will read this in the record.

Mr. Gibbs: I will follow you.

STIPULATION AS TO CERTAIN FACTS

Mr. Michell: (Reading): "It is hereby stipulated and agreed by and between the parties hereto and by and between their respective Counsel of record that the following facts are true and may be accepted as evidence in this case, subject to objection, however, on the part of either party to their competency, relevancy or materiality.

1. On February 26, 1937 the value of the corpus of the property transferred in trust is $570,937.50. The annual

four per cent return thereon is equivalent to $22,837.50. Table A of Article XIX, regulation 79, 1936 edition, relating to gift tax under the Revenue Act of 1932, (as amended and supplemented by the Revenue Acts of 1934 and 1935) provides for a factor of 14.11860 at the age of forty-four. Mrs. Smith was forty-four years of age at her nearest Birthday at the date of the execution of the trust indenture. The $22,837.50 yield at four per cent when multiplied by 14.11860 produces $322,433.53, which is the value of the life estate at the date of the execution of the trust instrument on the above basis.

The gift tax due on such basis, less the exemption of $45,000.00 is $31,565.03.

[fol. 25] 2. On February 26, 1937 there were deposited under the trust indenture and pursuant to its terms 3,000 shares of the six per cent cumulative convertible preferred stock, par value $100.00 per share of the L. C. Smith & Corona Typewriters Inc., yielding an annual income at the date of said trust of $18,000.00. Said issue of six per cent preferred stock has continued to pay six per cent dividends annually ever since.

On the basis of the annual income upon said trust fund of said sum of $18,000.00 a year, less $500.00 trustee's commissions allowed by law, the value of the life estate of Gladys D. Smith under the said trust indenture, using the same age and the factor of 14.11860 as was used in subdivision 1 above, is $247,075.50. The gift tax due on such basis, less the exemption of forty-five thousand dollars, is $20,261.33.

3. The gross income of the trust in question, less trustee's fees and payments to beneficiaries, was as follows:

Year	Gross Income	Trustee's Fees	Payments to Ben.	Balance
2-27-37 to 12-31-37	$20,250	$556.25	$19,693.75	00
1938	15,000	425.00	14,575.00	00
1939	7,500	237.50	7,262.50	00

On September 23, 1937 the three thousand shares of convertible preferred stock constituting the trust fund was converted by the Trustee into 15,000 shares of the common stock of L. C. Smith & Corona Typewriters Inc. Dividends

paid on April and July 1st, 1937 amounting to $4,500.00 each were paid on 3,000 shares of preferred stock. Divi- [fol. 26] dends paid on October 1st, 1937 and thereafter were paid on 15,000 shares of common stock."

Now there is a part 4 of this stipulation which I desire to object to as to the competency, relevancy and materiality. I will read it but I do object to it on the ground it is neither competent, relevant or material.

The Court: You read it and I will reserve decision on your objection.

Mr. Michell: (Reading) "4. That the Plaintiff, Hurlbut W. Smith was seventy-two years of age at his nearest birthday on February 26, 1937."

And if Your Honor should decide that it was material or relevant or competent Your Honor will give me an exception to your ruling?

The Court: Yes.

Mr. Gibbs: The Government wishes to object for the same reason for the matter stated in paragraphs 2 and 3.

The Court: All right. I will reserve decision on the objection, and if I rule against you you may have an exception.

Mr. Michell: That is our evidence.

Mr. Gibbs: The Government has no evidence. That is settled by the stipulation.

Motion to Amend Complaint

Mr. Michell: If the Court please: I move to amend the complaint to conform with the evidence offered.

Mr. Gibbs: No objection. We would amend the answer pursuant to the amended complaint.

The Court: Granted.

[fol. 27] Mr. Tompkins: Your Honor: I think the Plaintiff ought to make a statement of what the claim is.

Mr. Michell: We claim the balance of the gift tax.

Mr. Tompkins: What becomes of it, the balance of the tax?

Mr. Michell: Well the balance of the tax we claim is returnable to the Plaintiff.

The Court: I take it the tax was paid by Mr. Smith not from the trust fund, is that right?

Mr. Michell: It was paid by Mr. Smith personally and not from the trust fund.

Mr. Aylesworth: Our contention, briefly, is this: We paid the tax on the entire corpus of the trust fund. We claim that we only owe the Government a gift tax on the life estate and that we are entitled to a refund of the balance which we paid.

The Court: What I was asking, the tax was not paid from the trust fund in any way.

Mr. Michell: Oh no.

The Court: It was paid by Mr. Smith.

Mr. Aylesworth: Yes.

Mr. Gibbs: The allegations are to that effect and there is no contradiction of that. We admit that.

NOTE RE PLAINTIFF'S EXHIBIT 1

Trust Indenture. Printed in Schedule A of Complaint.

[fol. 28] PLAINTIFF'S EXHIBIT 2

Form 709.
Treasury Department.
Internal Revenue Service.
Revised October 1936.

Gift Tax Return

Calendar Year 193—

(To be filed in duplicate under the provisions of the Gift Tax Act of 1932, as amended)

Received Filed March 15, 1938.

Name of Donor Hurlbut W. Smith.
Address 1111 James Street, Syracuse, N. Y.
Citizenship U. S. A.
Residence U. S. A.

Have you (the donor), during the calendar year indicated above, without an adequate and full consideration in money or money's worth, made any transfer exceeding

$5,000 in value (or regardless of value if a future interest) as follows? (Answer "Yes" or "No.")

1. By the creation of an irrevocable trust for the benefit of another; Yes.

2. By making additions to an irrevocable trust previously created for the benefit of another .....;

3. By permitting a beneficiary (other than yourself) to receive the income from a revocable trust, where you possessed the power of revocation and chose during the year not to exercise it, whether such trust was created before or after the enactment, on June 6, 1932, of the Gift Tax Act of 1932 .....;

4. By relinquishing a power to revoke a trust created for the benefit of another .....;

[fol. 29] 5. By permitting another to withdraw funds from a joint bank account which were deposited by you .....;

6. By irrevocably assigning a life insurance policy, or by naming a beneficiary of a policy without retaining any of the legal incidents of ownership therein .....;

7. By paying a premium under an insurance policy in which you retain none of the legal incidents of ownership and the proceeds of which are payable to a beneficiary other than yourself or your estate .....;

8. By conveying title to another and yourself as joint tenants or to your wife or husband and yourself as tenants by the entirety .....;

9. By any other method, direct or indirect .....

If the answer is "Yes" to any of the foregoing, such transfer should be fully disclosed under schedule A or B.

Computation of Amount of Net Gifts for Year

1. Amount of gifts for year other than charitable, etc., gifts (item *c*, schedule A)	$570937.50	
2. Amount of charitable, public, and similar gifts for year (item *c*, schedule B)	4705.21	
3. Total amount of gifts for year (item 1 plus item 2)		$575642.71
4. Amount of charitable, public, and similar gifts for year (item *c*, schedule B)	$4705.21	

5. Specific exemption claimed (see instructions)	45000.00	
[fol. 30] 6. Total deductions (item 4 plus item 5)		$9705.21
7. Amount of net gifts for year (item 3 minus item 6)		$525937.50

Computation of Tax

1. Amount of net gifts for year (item 7, above)	$525937.50
2. Total amount of net gifts for preceding years (item *c*, schedule C)	None
3. Total net gifts (item 1 plus item 2)	$525937.50
4. Tax computed on item 3	
5. Tax computed on item 2	
6. Tax on net gifts for year (item 4 minus item 5) Paid—3/15/38	$71674.22

Affidavit

I swear (or affirm) that this return, including the accompanying schedules and statement, if any, has been examined by me, and to the best of my knowledge and belief, is a true, correct, and complete return for the calendar year stated, pursuant to the Gift Tax Act of 1932, as amended, and the regulations issued thereunder, and no transfer required by said law and regulations to be returned other than the transfer or transfers disclosed herein under schedules A or B was made by me (the donor) during said calendar year.

(Signed) Hurlbut W. Smith, H. W. S. (Signature of donor/executor).

[fol. 31] Sworn to and subscribed before me this 15th day of March, 1938. J. M. K. (Signed) Judith Mills Klist, Notary Public. (Seal.) (Signature and title of officer administering oath.) (Notarial Seal.)

Affidavit

I swear (or affirm) that I prepared this return for the person named herein and that this return, including the accompanying schedules and statements, if any, is a true, correct, and complete statement of all the information respecting the donor's gift tax liability of which I have any knowledge.

(Signed) Judith Mills Klist, Secretary, J. M. K. C/o L. C. Smith & Corona Typewriter Inc., Syracuse, N. Y. (Address of person preparing return).

Sworn to and subscribed before me this 15th day of March, 1938. (Signed) Henry A. Eiler, Notary Public. (Seal.) (Signature and title of officer administering oath.) (Notarial Seal.)

Schedule A.—Gifts During Year Other Than Charitable, Public, and Similar Gifts

Item No.	Description of Gift, Motive, and Donee's Name and Address	Date of Gift	Value at Date of Gift
	3000 shares of the convertible preferred stock of L. C. Smith & [fol. 32] Corona Typewriters Inc., a corporation organized under the *the* laws of the State of New York on October 30, 1924, of the par value of $100 per share, returned at a quotation of $190.3125 per share. The stock is unlisted. The location of the principal business office in New York State is 701 East Washington Street, Syracuse, N. Y. The Donee is The Syracuse Trust Company, Trustee under an agreement in writing dated February 26, 1937, a copy of which is hereto annexed and marked "A", and the motive was to provide an income for Gladys D. Smith during her lifetime, with the remainder to her benefici-	2/26/37	$570937.50

aries upon her death, with reversion to the Donor in the event of his survivorship. The net income of said trust for the year 1937 amounted to $19693.75.

(a) Total	$570,937.50
(b) Less total exclusions not exceeding $5,000 for each donee (except future interests)	5,000.00
(c) Included amount of gifts for year other than charitable, etc., gifts	$565,937.50

Schedule B.—Charitable, Public, and Similar Gifts During Year

[fol. 33] Contributions

• • • • • • •

1937

• • • • • • •

Gift Tax Return Form 709
Schedule B

Syracuse Community Chest	$99.26
Betts Memorial Universalist Church	634.50
American Red Cross	100.00
St. Larence University	300.00
Sagola Home	50.00
Syracuse University Alumni Fund	1000.00
Syracuse University	909.00
Syracuse University—Syracuse-in-China	10.00
Young Men's Christian Association	200.00
Rotary Club Charity Fund	50.00
Syracuse Museum of Fine Arts	100.00
Christian Endeavor Convention	50.00
National Recreation Assn.	25.00
National Probation Assn.	10.00
St. Vincent's Orphan Asylum	10.00
Ducks Unlimited (NY State Com.)	30.00
Bethany Baptist Church	5.00
Christian Youth Syracuse Council of Churches	33.75
Lisle Congregational Church	130.00
Ladies Aid Otselic Church	5.00
New York State Conference on Social Work	10.00
Central New York S. P. C. A.	10.00

Syracuse Foundation	5.00
Ozark Mountain School	5.00
Shriners Hospital Fund	2.00
[fol. 34] Onondaga Health Seals	1.00
The Northfield Schools—Cash	1.00
Rev. Frank Hopps—Hamlet Chapel—Cash	10.00
Church of Christ—Cash	5.00
	$4705.21

Schedule C.—Returns, Amounts of Specific Exemption, and Net Gifts for Preceding Years (Subsequent to June 6, 1932) None.

PLAINTIFF'S EXHIBIT 3

Syracuse, N. Y. March 15, 1938 No. 28974

Pay to the Order of Collector of Internal Revenue at Syracuse, New York $71,674.22

Seventy-one thousand six hundred seventy-four and 22/100 —Dollars in full payment as follows

HURLBUT W. SMITH

(Rubber Stamp)

This check is in payment of an obligation to the United States and must be paid at par. No protest. 1-120

To the Syracuse Trust Company, Syracuse, N. Y. 50-42

(Perforation)

Paid 3-18-38 50-42

H. W. Smith

(Rubber Stamp on back of Check)

This check is in payment of an obligation to the United States and must be paid at par. No Protest. Mar. 16, 1938. [fol. 35] F. J. Shaughnessy, Collector of Internal Revenue, 21st District of New York.

Pay to the Order Any Bank, Banker or Tust Co. Prior Endorsement. Guaranteed.

Received Payment

Through Syracuse Clearing House

Mar 18 1938

Prior Endorsements Guaranteed

MERCHANTS NATIONAL BANK & TRUST CO.

Syracuse, N. Y.

R. E. Ashpole, Cashier.

NOTE RE PLAINTIFF'S EXHIBIT 4

Claim for Refund. Printed in Schedule A of Complaint.

NOTE RE PLAINTIFF'S EXHIBIT 5

Commissioner's letter respecting claim for Refund. Printed in Schedule B of Complaint.

[fol. 36] IN UNITED STATES DISTRICT COURT, NORTHERN DISTRICT OF NEW YORK

HURLBUT W. SMITH, Plaintiff,

against

FRANK J. SHAUGHNESSY, Collector of Internal Revenue of the United States for the Twenty-first District of New York, Defendant

APPEARANCES:

Messrs. Mackenzie, Smith & Michell, attorneys, (Willis H. Michell, Esq., and Basil B. Aylesworth, Esq. of counsel), for the Plaintiff.

Ralph L. Emmons, Esq., United States Attorney, (B. Fitch Tompkin, Esq., Asst. U. S. Attorney, and Julian G. Gibbs, Esq., Spec. Asst. to Attorney General, of counsel.) for the Defendant.

OPINION—Filed July 15, 1941

BRYANT, D. J.:

This is an action for recovery of gift taxes paid during the year 1937.

On February 26th, 1937, plaintiff executed a trust indenture to the Syracuse Trust Company as Trustee, whereby he established a trust fund consisting of 3000 shares of the 6% convertible preferred stock of the L. C. Smith & Corona Typewriters, Inc., and provided that the income from the said trust fund should be paid to his wife for life with remainder, upon her death, to himself if living, and, [fol. 37] if not then living, to her legatees or, if she died intestate, to her distributees.

On March 15, 1938, plaintiff filed a Federal Gift Tax return of said transfer, showing a value of the trust fund of $570,937.50 and a net taxable gift of the entire fund, after deductions of exemptions, of $525,937.50 and paid a gift tax thereon of $71,674.22. He almost immediately thereafter filed a claim for refund upon the ground that the transfer set forth in the trust indenture did not constitute a taxable gift. On April 15th, 1938, the commissioner rejected said refund claim in its entirety and thereafter this action to recover was timely brought.

Defendant, in his brief, sets forth four questions which he states the issues raised. Possibly time will be saved by answering these questions more or less categorically.

1. Did a transfer of securities by an irrevocable transfer in trust in this case constitute a taxable gift, under the federal gift tax statute, measured by the value of the securities in question in their entirety as of the date of execution of the trust instrument?

Upon the authorities of Klein v. United States, 283 U. S. 231, and Helvering v. Hallock, 309 U. S. 106, I hold that the transfer did not constitute a taxable gift measured by the value of the securities as of the date of the execution of the trust investment.

2. Are the gift taxes and the estate tax statutes *in pari materia*, or are they mutually exclusive?

The two statutes are not mutually exclusive, but are considered *in pari materia*. (Sanford v. Commissioner, 308 U. S. 39; Walker v. Commissioner, 40 B. T. A. 762).

3. If a taxable gift was not effected as contemplated in (1) above, then did the transfer give rise to a taxable gift, [fol. 38] measured by the commuted value of the wife's life interest as of the date of execution of the instrument?

Yes. Under the provisions of said trust indenture the wife received a complete and absolute gift of a life interest in said trust fund. This taxable gift should be measured by the value of the wife's life interest as of the date of the execution of the instrument.

4. If the transfer gave rise to a taxable gift as contemplated in (3) above is the commuted value of the wife's life interest to be computed on the basis of a 4% annual

return pursuant to the official Regulations, or on the basis of an actual annual 6% return on the securities involved, and is the refund claim sufficient to raise such question?

The question as framed by defendant could easily mislead. Both methods of computation, rather than one, set forth in the question are provided for in the official Regulations. The cash value of the wife's life interest should be computed according to the provisions of Subd. g, Sec. 85.19, Chap. 1, Title 26 of the Code of Federal Regulations. The portion of subdivision g, which seems to be applicable, reads:

"If a gift consists of the donor's right to receive the entire income of certain property during the life of Z, or for a term of years, and the annual rate of income for a period equal to or exceeding the life expectancy of Z, or for such term of years, is fixed or definitely determinable at the time of the gift, then the value of the gift should be computed as explained above in the case of an annuity. If the rate of annual income is not determinable, or if the donor is entitled merely to the use of nonincome-producing [fol. 39] property, a hypothetical annuity at the rate of 4 percent of the value of the property should be made the basis of the calculation."

It was stipulated that the stock (convertible preferred 6% stock) yielded an annual income of $18,000.00 at the time of the making of the trust indenture and that it has paid 6% since that time. The stipulation further shows that the trustee's commissions allowed by law amount to $500.00 per year, and that the wife's expectancy of life, at the time of the making of the trust was 14:11860.

It is plaintiff's contention that the income "was fixed and definitely determinable at the time of the gift." He claims a fixed maximum annual income of $17,500.00 ($18,000.00 income less $500.00 commissions), and that the value of the life interest should be computed by multiplying $17,500.00 by the above mentioned factor. This computation makes the value of the life interest $247,075.50. On that valuation the tax amounts to $20,261.33.

Defendant says there was not "a fixed or definitely determinable annual rate of income" at the time of transfer. He contends that the value of the life interest must be computed as provided in the last part of the quoted portion of

the subdivision, that is by multiplying 4% of the full value of the stock at time of transfer (which was $570,937.50) by the above mentioned factor. Computed under this method the life interest had a value of $322,433.53. The gift tax on such valuation amounts to $31,565.03.

My answer is in favor of defendant's contention. Were it not for the convertible feature, I would answer directly the opposite. The tax should be computed upon the same basis that the Commissioner would have computed it, had he taxed the value of a life interest only. The taxable gift [fol. 40] was donor's right to receive the dividends on the stock transferred, or stock received on conversion thereof, during the period of his wife's left expectancy. The annual income therefrom could not then be definitely ascertained. Without conversion the income was fixed, but through conversion it might be more or less. To hold that donor can give a life interest in preferred convertible stock and satisfy the taxing statute by paying a tax on value computed on rate of preferred dividend, when the trustee can, the next day, convert into stock that may pay larger dividends, favors facile tax avoidance. That the trustee here had power to convert cannot be questioned because it has done so in part.

My holding on method of computation obviates the necessity of answering the last part of question (4).

Upon the trial the defendant objected to paragraphs 2 and 3 of the stipulation of facts upon the ground that the same were immaterial, irrelevant and incompetent. I reserved decision. I now over-rule the objection. The defendant is entitled to exceptions thereto. The plaintiff objected to paragraph four of the stipulation of facts on the same grounds. I now sustain the objection. Defendant is entitled to an exception. I see no necessity for here quoting the paragraph ruled upon.

Plaintiff is entitled to judgment for the sum of $40,109.19 with interest and costs.

Findings of material facts and Conclusions may be presented on notice.

Dated: July 14th, 1941.

Frederick H. Bryant, United States District Judge.

[fol. 41] IN DISTRICT COURT OF THE UNITED STATES, NORTHERN DISTRICT OF NEW YORK

[Title omitted]

Findings of Fact and Conclusions of Law—Filed September 10, 1941

The issues of fact and law in the above entitled action having been tried by the court without a jury at a Regular Term of the United States District Court held in and for the Northern District of New York, at the Federal Building, Syracuse, New York, on October 28, 1940, and the evidence and proofs of the parties having been taken, and after hearing Willis H. Michell, and Basil B. Ayleworth, of Mackenzie, Smith & Michell, Solicitors for plaintiff, and B. Fitch Tompkins and Julian G. Gibbs, of counsel, and Solicitors for defendant, and after due consideration of the evidence and the briefs submitted by the parties, the court hereby decides, and makes findings of fact and conclusions of law, as follows:

FINDINGS OF FACT

1. That the plaintiff is a citizen of the State of New York and of the United States, and a resident of the City of Syra-
[fol. 42] cuse, County of Onondaga and State of New York, and of the Northern District of New York.

2. That at all times herein mentioned the defendant Frank J. Shaughnesy was and now is a resident of the City of Syracuse, County of Onondaga and State of New York and of the Northern District of New York, and was and now is the duly appointed, qualified and acting Collector of Internal Revenue of the United States for the Twenty-first District of New York.

3. That on the 26th day of February, 1937, pursuant to and by the provision of a Trust Indenture dated on that day, executed by and between the plaintiff and The Syracuse Trust Company, a banking corporation of Syracuse, New York, the plaintiff assigned, transferred and set over irrevocably unto said The Syracuse Trust Company and its successors three thousand (3000) shares of the convertible preferred stock of L. C. Smith & Corona Typewriters, Inc., a New York Corporation, having its principal office and place for the transaction of business in the City of Syra-

cuse, New York, in trust nevertheless, to manage and control said property and to keep the same or the proceeds thereof invested and to collect the income thereof and to pay over the net income from said trust fund quarterly to and for the use of Gladys D. Smith, wife of the plaintiff, during her life, and upon her death, to pay over the principal of said trust fund to the plaintiff, if he be then living, or in the event of the death of the plaintiff, prior to the death of his said wife, to pay over said principal of said trust to such person or persons and in such amounts and proportions as the said life beneficiary should by her last Will and Testament direct, and in the event of her failure to make a testamentary disposition thereof, then to such per- [fol. 43] son or persons and in such amounts and proportions as would take the same under the laws of the State of New York in case the principal of said trust fund had been owned outright by the said life beneficiary and she had died intestate.

4. That thereafter and on March 15, 1938, the plaintiff made and filed with the defendant, Collector for the Twenty-First District of New York, a return of said transaction and transfer for gift tax purposes showing the full value of the principal of said trust fund on February 26, 1937, the date of the creation of said trust fund, of $570,937.50.

5. That upon said return, and upon said full value of said trust fund, after deducting therefrom the exemption of $40,000 and the exclusion of $5,000 claimed by plaintiff in said return, the defendant, Collector as aforesaid, assessed a federal gift tax in the amount of $71,674.22, which tax was paid by the plaintiff to said defendant, Collector as aforesaid, on March 15, 1938, by plaintiff's check, payment on which was completed through Syracuse Clearing House on March 18, 1938.

6. That on March 18, 1938, the plaintiff filed with the defendant, Collector as aforesaid, a duly verified claim, in form as approved by law, for the refund of said gift tax so assessed, collected and paid, on the ground that the transfer set forth in said Trust Indenture did not constitute a taxable gift.

7. That thereafter and on April 15, 1938, the Commissioner of Internal Revenue rejected said claim for refund

in its entirety, and notified the plaintiff of such rejection by letter forwarded by registered mail, which letter of rejection was deliverd to and received by plaintiff on or about April 16, 1938.

[fol. 44] 8. That this action was commenced by the issuance and personal service of the summons, with the complaint herein, on March 14, 1940, and within the time permitted by law.

9. That the full value of said trust fund on the date of the execution of said Trust Indenture was $570,937.50.

10. That the annual rate of income from said trust fund for a period equal to the life expectancy of said Gladys D. Smith was not fixed or definitely determinable at the date of the execution of said Trust Indenture because the trust property was convertible, and that the value of the life interest of said Gladys D. Smith in said trust fund should be computed upon the basis of a hypothetical annuity at the rate of 4% upon the value of said trust fund on the date of the execution of said Trust Indenture.

11. That the trustees' commissions upon the annual income of said trust fund at the date of the execution of said Trust Indenture, as allowed by law and as stipulated herein, amounted to $500. and should be deducted from the amount of the hypothetical annuity in computing the value of said life interest.

12. That on February 26, 1937, the date of the execution of said Trust Indenture, said Gladys D. Smith was 44 years of age at her nearest birthday.

13. That the expectancy of life of said Gladys D. Smith on February 26, 1937, was 14.11860 years, which is the factor to be used in computing the value of her life interest in said Trust Fund.

14. That the value of the life interest of Gladys D. Smith in said trust fund at the date of the execution of said Trust Indenture, as stipulated herein, was $322,433.53.

15. That the plaintiff is entitled to an exemption of $40,-
[fol. 45] 000 and an exclusion of $5,000 from said value of said life estate, in computing the gift tax thereon.

16. That the federal gift tax on the transfer of said life interest to Gladys D. Smith, as stipulated herein, amounts to the sum of $31,565.03.

17. That the difference between the amount paid by the plaintiff as gift tax on the entire interest in said trust fund, and the amount of the gift tax on said life interest therein is $40,109.19.

CONCLUSIONS OF LAW

1. That under the provisions of said Trust Indenture, the transfer of said securities pursuant thereto did not constitute a taxable gift measured by the total value of said securities.

2. That under the provisions of said Trust Indenture, there was thereby made a complete and absolute gift of a life interest in said trust fund to Gladys D. Smith.

3. That the transfer of said life interest to Gladys D. Smith constituted a taxable gift, the amount of which for gift tax purposes is measured by the value of said life interest as of the date of the execution of said Trust Indenture.

4. That the value of said life interest of Gladys D. Smith should be computed upon the basis of a hypothetical annuity at the rate of 4 per cent upon the value of the trust fund on the date of the Trust Indenture.

5. That a federal gift tax upon the transfer of said life interest to Gladys D. Smith in the sum of $31,565.03 as stipulated herein, became due and payable to the defendant.

6. That the plaintiff is entitled to recover from the defendand the amount paid by plaintiff as gift tax, less said [fol. 46] amount of the gift tax due upon the transfer of said life estate, such balance amounting to the sum of $40,109.19, and to have judgment against the defendant for said sum of $40,109.19, with interest from March 18, 1938 until payment thereof, and costs. Judgment is directed to be entered accordingly.

Dated: September 9, 1941.

Frederick H. Bryant, United States District Judge.

In District Court of the United States, Northern District of New York

Hurlbut W. Smith, Plaintiff,

vs.

Frank J. Shaughnessy, Collector of Internal Revenue of the United States for the Twenty-first District of New York, Defendant

Civil Action File No. 386

Judgment—September 9, 1941

This cause having come on regularly for trial before the Court without a jury at a regular term of the United States District Court held in and for the Northern District of New York, at the Federal Building, Syracuse, New York, on October 28, 1940, and Mackenzie, Smith & Michell, Esqs., appearing as Solicitors for Plaintiff, by Willis H. Michell [fol. 47] and Basil B. Aylesworth, and Ralph L. Emmons, Esq., United States Attorney, appearing as Attorney for Defendant, by B. Fitch Tompkins and Julian G. Gibbs, of Counsel; and the trial having been proceeded with and evidence on behalf of the parties having been introduced and closed, and the cause having been submitted to the Court for consideration and decision; and the Court, after due deliberation, having rendered its decision and filed its Findings of Fact and Conclusions of Law and ordered that judgment be entered in accordance with said Findings and Conclusions;

Now, on motion of Mackenzie, Smith & Michell, Solicitors for Plaintiff, it is

Adjudged that the plaintiff above named, Hurlbut W. Smith, do have and recover of and from the defendant above named, Frank J. Shaughnessy, Collector of Internal Revenue of the United States for the Twenty-first District of New York, the principal sum of Forty Thousand One Hundred Nine Dollars and Nineteen Cents ($40,109.19) with interest thereon from March 18, 1938, until paid at the rate of six percent (6%) per annum, and the sum of Twenty-four Dollars and Sixty Cents ($24.60), costs of this proceeding this day taxed by the Clerk of this Court.

Done and ordered at Syracuse, N. Y., this 9 day of September, 1941.

Frederick H. Bryant, United States District Judge.

[fols. 48-49] Bill of costs omitted in printing.

[fol. 50] In United States District Court, Northern District of New York

[Title omitted]

Certification by Judge Bryant—Filed September 11, 1941

I, Frederick H. Bryant, United States District Judge, before whom the above action was tried, do hereby certify that the defendant is a revenue officer of the United States, Collector of Internal Revenue, District No. 21; and for all his acts in respect to the matter in suit he had probable cause and acted under the laws of the United States and direction of the United States Secretary of the Treasury and other proper officers of the United States.

Dated: September 8, 1941.

Frederick H. Bryant, United States District Judge.

[fol. 51] In United States District Court, Northern District of New York

[Title omitted]

Notice of Appeal—December 9, 1941

Notice Is Hereby Given that Frank J. Shaughnessy, Collector of Internal Revenue for the Twenty-first District of New York, defendant above named, hereby appeals to the Circuit Court of Appeals for the Second Circuit from the final judgment entered in this action on the 10th day of September, 1941.

Dated, December 9, 1941.

Ralph L. Emmons, United States Attorney and Attorney for Appellant, Address: Federal Building, Binghamton, N. Y.

To Glen A. Porter, Clerk, U. S. District Court, Utica, N. Y. Mackenzie, Smith & Michell, Attorneys for Plaintiff, 821 Onondaga County Savings Bank Bldg., Syracuse, N. Y.

[fol. 52] In District Court of the United States, Northern District of New York

[Title omitted]

Points to be Relied Upon on Appeal

Comes now the defendant, by his attorney, Ralph L. Emmons, United States Attorney, and files the following as his points to be relied upon on appeal:

1. Plaintiff, on February 26, 1937, established an irrevocable trust, the income from which was payable to his wife for life. Upon her death the principal reverts to the settlor, if living, or if he be not living, then to his wife's appointees or next of kin. Plaintiff paid a gift tax on the assumption that the full value of the securities transferred to the trust was subject to gift tax. In the District Court he contended that the tax had been erroneously paid on the ground that the transfer in trust did not constitute a completed gift. The defendant contended that the transfer constituted a taxable gift measured by the full value of the properties transferred. The Court held that the value of the wife's life estate only was subject to the tax. The Court erred in so holding.

[fol. 53] 2. The Court erred in not holding that the entire value of the securities transferred to the trust, less only the grantor's reversionary interest, is subject to the tax.

3. The Court erred in entering judgment for plaintiff.

Ralph L. Emmons, United States Attorney.

In United States District Court, Northern District of New York

[Title omitted]

Order Extending Time to File Record—Filed January 13, 1942

On application of the United States of America, appellant in the above action, and under provisions of Rule 73, it is

Ordered that the time within which the appellant shall file the record on appeal with the Circuit Court of Appeals for the Second Circuit herein is hereby extended to March 5th, 1942.

[fol. 54] Dated: January 10, 1942.

Frederick H. Bryant, United States District Judge.

In United States District Court, Northern District of New York

[Title omitted]

Stipulation as to Record

It is hereby Stipulated that the foregoing printed record contains a full, true and correct record of the pleadings necessary for the determination of the appeal herein, including the opinion or decision of the United States District Judge filed herein and that the Clerk of the U. S. District Court for the Northern District of New York, shall make return thereof and file the same with the United States Circuit Court of Appeals for the Second Circuit without further comparison as and for a complete and true transcript of the record on the appeal in said cause.

[fol. 55] Dated February —, 1942.

Ralph L. Emmons, United States Attorney for the Northern District of New York, Attorney for Defendant-Appellant. Mackenzie, Smith & Michell, Attorneys for Plaintiff-Appellee, 821 Onondaga County Savings Bank Bldg., Syracuse, New York.

[fol. 56] Clerk's Certificate to foregoing transcript omitted in printing.

[fol. 57] IN UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

(Argued May 20, 1942)

HURLBUT W. SMITH, Appellee,

v.

FRANK J. SHAUGHNESSY, Collector, Appellant

On appeal from a judgment of the District Court for the Northern District of New York in favor of the plaintiff, in an action to recover taxes wrongfully collected.

Before L. Hand, Augustus N. Hand and Chase, Circuit Judges

L. W. Post for the appellant.
Basil B. Aylesworth for the appellee.

OPINION—June 19, 1942

Per Curiam:

Reversed and complaint dismissed on the authority of *Herzog* v. *Commissioner*, 116 Fed. (2d) 591 (C. C. A. 2).

[fol. 58] IN UNITED STATES CIRCUIT COURT OF APPEALS, SECOND CIRCUIT

HURLBUT W. SMITH, Plaintiff-Appellee,

v.

FRANK J. SHAUGHNESSY, Collector, etc., Defendant-Appellant

JUDGMENT—July 6, 1942

Appeal from the District Court of the United States for the Northern District of New York

This cause came on to be heard on the transcript of record from the District Court of the United States for the Northern District of New York, and was argued by counsel.

On Consideration Whereof, it is now hereby ordered, adjudged, and decreed that the judgment of said District

Court be and it hereby is reversed with costs and cause remanded with a direction to dismiss the complaint.

It is further ordered that a Mandate issue to the said District Court in accordance with this decree.

D. E. Roberts, Clerk.

[fol. 59] Clerk's Certificate to foregoing transcript omitted in printing.

[fol. 60] SUPREME COURT OF THE UNITED STATES, OCTOBER TERM, 1942

No. 429

ORDER ALLOWING CERTIORARI—Filed November 9, 1942

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Second Circuit is granted, and the case is transferred to the summary docket.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

Endorsed on Cover: File No. 46930. U. S. Circuit Court of Appeals, Second Circuit. Term No. 429. Hurlbut W. Smith, Petitioner, vs. Frank J. Shaughnessy, Collector of Internal Revenue of the United States for the Twenty-first District of New York. Petition for a writ of certiorari and exhibit thereto. Filed September 29, 1942. Term No. 429. O. T. 1942.

No. 429

SEP 29 1942
CHARLES ELMORE CROPLEY

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1942

HURLBUT W. SMITH,
Petitioner and Appellee below,

vs.

FRANK J. SHAUGHNESSY, Collector of Internal Revenue of the United States for the Twenty-first District of New York,
Respondent and Appellant below.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT AND BRIEF IN SUPPORT THEREOF.

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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1942

No.

HURLBUT W. SMITH,
Petitioner and Appellee below,

vs.

FRANK J. SHAUGHNESSY, Collector of Internal Revenue of the United States for the Twenty-first District of New York,
Respondent and Appellant below.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT AND BRIEF IN SUPPORT THEREOF.

To the Honorable Chief Justice and Associate Justices of the Supreme Court of the United States:

Petitioner prays that a writ of certiorari issue to review the judgment of the Circuit Court of Appeals for the Second Circuit entered on July 6, 1942, reversing the judgment of the District Court of the United States for the Northern District of New York entered September 10, 1941, and respectfully shows as follows:

OPINIONS BELOW

The opinion of the District Judge upon the trial of the case is printed at page 36 of the Record, and is reported in 40 Fed. Sup. 19. The Circuit Court of Appeals handed down a memorandum decision printed at page 57 of the Record, and reported in 42-2 U. S. T. C., Par. 10, 194.

JURISDICTION

The jurisdiction of this Court to review this decision is derived from Section 240 of the Judicial Code as amended (28 U. S. C. A., Sec. 347), wherein this Court is authorized upon the petition of any party to require by certiorari either before or after a judgment or decree by such lower Court, that the cause be certified to the Supreme Court for determination by it, with the same power and authority and with like effect as if the cause had been brought by unrestricted writ of error or appeal.

This case involves the interpretation of Sections 501 and 510 of the Revenue Act of 1932, c. 209, 47 Stat. 169.

The decision which petitioner seeks to have reviewed was handed down by the Circuit Court of Appeals for the Second Circuit on June 19, 1942.

STATEMENT OF MATTER INVOLVED

This action was instituted in the United States District Court for the Northern District of New York by Huribut W. Smith, petitioner herein, against the defendant, to recover for gift taxes alleged to have been illegally and erroneously assessed against and exacted from petitioner. The taxes were assessed and paid, in the sum of $71,674.22, upon the entire corpus of a trust fund created under a Trust Indenture dated February 26, 1937, whereby the petitioner transferred certain shares of stock to The Syracuse Trust Company, as Trustee, and directed the distribution of the principal and income thereof as follows:

"To pay over the net income from said trust fund quarterly to and for the use of Gladys D. Smith, wife of the Settlor (hereinafter sometimes called the 'Life Beneficiary'), during her natural life, and upon her death to pay over the principal of said trust fund to the Settlor, Hurlbut W. Smith, if he is then living, or in the event of the death of said Settlor prior to the death of the Life Beneficiary to pay over said principal of said trust fund as follows:

The Trustee shall upon the death of said Life Beneficiary pay over the principal of said trust to such person or persons and in such amounts and proportions as the said Life Beneficiary may by her last will and testament direct, and in the event of her failure to make testamentary disposition thereof, then and in that event the principal of the trust herein created for her life shall be paid over and delivered by the Trustee to such person or persons and in such amounts and proportions as would take the same under the laws of the State of New York in case the principal of said trust fund had been owned outright by the said Life Beneficiary and she had died intestate."

A certified copy of the entire record of the case in the Circuit Court of Appeals is hereby furnished as a part of this application in conformity with Rule 38 of this Court relative to cases from the Circuit Court of Appeals.

The case was tried by the Court without a jury and findings of fact and conclusions of law made by the Court whereby it was held in effect that the only taxable gift under the Trust Indenture was the value of the life interest of Gladys D. Smith, the wife of petitioner, and that the plaintiff was entitled to recover from the defendant the sum of $40,109.19 with interest,

being the amount of the tax paid by him less the amount of tax computed upon said life interest of Gladys D. Smith (R. 45, 46).

Judgment was granted for plaintiff for the said sum and entered in said action on September 10, 1941 (R. 47).

The defendant appealed from said judgment to the Circuit Court of Appeals, Second Circuit, by a notice of appeal dated December 9, 1941 (R. 51).

The principal questions raised on such appeal to the Circuit Court were (a) as to whether the District Court erred in holding that the value of the life interest of the wife under the Trust Indenture was the only interest created by said Indenture which was subject to gift tax, and (b) whether the District Court erred in not holding that the entire corpus of the trust fund, less only the value of donor's reversionary interest therein, was subject to gift tax (R. 52, 53).

The Circuit Court of Appeals reversed the decision of the lower Court on the authority of *Herzog vs. Commissioner*, 116 Fed. 2d, 591 (C. C. A. 2).

THE QUESTION PRESENTED

Whether there was a completed gift of the corpus or principal of the trust fund created by the Trust Indenture hereinabove quoted, which rendered the principal subject to gift tax. It was conceded and stipulated that the gift of the life estate was complete and absolute, and was subject to gift tax.

STATUTES AND REGULATIONS INVOLVED

The pertinent Statutes and Regulations are printed in the Appendix, *infra*.

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred in holding that a gift tax was payable upon all, or upon any part, of the corpus of the trust fund, for the following reasons:

(1) Because the Trust Indenture expressly provided that the principal should revert to the donor, if living at the death of the Life Beneficiary.

(2) Because the possible interests of the remaindermen (statutory distributees of the life tenant) are indeterminate, and are not capable of evaluation, either by deducting the value of the life estate and the reversionary interest of the taxpayer, computed on an actuarial basis, or by any other method. The general power of appointment of the principal precedes and is destructive of any measurable interest of said remaindermen.

(3) Because under the general power of appointment granted by the donor, the principal of the trust may be appointed by the life tenant to any alienee whatever, including tax-exempt charitable institutions.

REASONS RELIED ON FOR THE WRIT

1. The decision of the Circuit Court of Appeals for the Second Circuit, reversing the decision of the District Court, appears to be contrary to the applicable decisions of this Court, particularly in the Hallock and Sanford cases cited below.

It appears on the face of the Trust Indenture that the gift of the corpus of the trust fund was incomplete (and therefore not subject to gift tax), because the donor reserved the corpus to himself if he should survive the life beneficiary. The corpus of the trust fund is clearly subject to estate tax.

Helvering vs. *Hallock*, 309 U. S. 106.

Klein vs. *United States*, 283 U. S. 231.

Burnet vs. *Guggenheim*, 288 U. S. 280.

Ezequiu vs. *Humphreys*, 308 U. S. 54.

Helvering vs. *Hutchins*, 312 U. S. 393, 396.

Burdick vs. *Commissioner* (C. C. A. 2) 117 Fed. 2d, 972, Certiorari denied, Oct. 13, 1941.

In *Commissioner* vs. *Marshall*, 125 Fed. 2d, 843, the Court below held that where a gift was made in trust for a life beneficiary, the principal to revert to the donor if he survived the life tenant, otherwise with remainder over, the entire principal of the trust fund was subject to gift tax. Said decision appears to conflict with the decision of this Court in the *Hallock* case. In both cases the question was, did the donor completely part with the principal. The gift tax is predicated upon something *completely given up* to donees. The estate tax is predicated upon something *retained*. As held in the *Hallock* case, the donor may not be said to have parted with the principal until the event had occurred which determined whether the principal came back to the donor or passed to the remaindermen.

Furthermore, because the gift of the principal was incomplete, it will be subject to estate tax on the death of the donor, whether before or after the death of the life beneficiary.

Helvering vs. *Hallock*, 309 U. S. 106.

Burdick vs. *Commissioner* (C. C. A. 2) 117 Fed 2nd, 972, Certiorari denied Oct. 13, 1941.

The gift tax statute and the estate tax statute are in pari materia, and are supplementary in character. It is submitted

that the supplementary character of the gift and estate tax statutes was established by the decision in *Estate of Sanford* vs. *Commissioner*, 308 U. S. 39, as a general principle, subject only to certain necessary exceptions, and was not intended by that decision to be limited solely to the specific facts of the *Sanford* case, as held by the Court below in *Commissioner* vs. *Marshall*, 125 Fed. 2d, 948. The present case does not fall within the necessary exceptions to the general rule established in the *Sanford* case, and therefore, as the corpus of the trust fund, by reason of the provisions of the Trust Indenture, will be subject to estate tax on the death of the donor, it is not subject also to a gift tax under the same provisions. The very nature of the two taxes seems to preclude the imposition of both, under such circumstances.

The case of *Herzog* vs. *Commissioner* (116 Fed. 2d, 591), on the authority of which the Court below rendered its decision herein, is clearly distinguishable from the present case. In that case the donor had parted with all legal and equitable rights in both principal and income. Anything which the trustee might give him back was wholly discretionary. In the present case, no discretionary power is interposed between the donor and the corpus of the trust fund. If the donor survived the life beneficiary, it reverted to the donor automatically.

The decision of the Court below herein appears therefore to conflict with the decisions of this Court in the *Hallock* and *Sanford* cases.

2. The Circuit Court of Appeals for the Second Circuit has herein decided an important question of federal law which has not been decided by this Court unless to the contrary, and which should be finally settled beyond question by this Court.

This question involves the interpretation of the gift tax statute, as affected by Section 510, which provides as follows:

> "The tax imposed by this title shall be a lien upon all gifts made during the calendar year, for 10 years from the time the gifts are made. If the tax is not paid when due, the donee of any gift shall be personally liable for such tax to the extent of the value of such gift * * *."

The donor herein did not give the principal of the trust fund to *determinable remaindermen*, subject merely to the reversion of the principal to himself if he survives the life tenant. He provided that the principal of the trust should pass, first to the appointees of the life tenant under a general power of appointment by will, and second, and only in case of the failure of such appointment, to the distributees of the life tenant under the New York statute of distribution.

Under said general power granted by the donor, the life tenant may appoint the principal of the trust fund to *any alienee whatsoever, including tax-exempt educational and charitable institutions*, without any limitation, and according to her mere whim or fancy, and thus cut off and destroy the interests of her statutory distributees, as remaindermen.

Farmers Loan and T. Co. vs. Shaw, 127 App. Div. 656, 660; Affmg. 56 Misc. 201.

Matter of McDonagh, 18 Ont. W. N. (Ontario Weekly Notes) 154.

Cutting vs. Cutting, 86 N. Y. 522, 530-531.

Dana vs. Murray, 122 N. Y. 604, 612.

Matter of Moehring, 154 N. Y. 423, 427.

New York Real Property Law, Sec. 134 (Also applicable to personal property, *Matter of Moehring*, 154 N. Y. 423, 427).

The federal authorities are to the same effect.

Morgan vs. Commissioner, 309 U. S. 78.

Treasury Regulations 80 (1937 Ed.) Art. 24.

It thus appears that the potential interests of the distributees of the life beneficiary, as presumptive remaindermen, are wholly dependent upon the mere whim or fancy of a human being, and even further, that the principal of the trust fund may pass, under the general power granted by the donor, to tax-exempt educational or charitable institutions. The potential interests of these remaindermen are therefore impossible of measurement, and have no value which is ascertainable by any known actuarial methods.

Humes vs. United States, 276 U. S. 487.

Ithaca Trust Co. vs. United States, 279 U. S. 151.

Helvering vs. Blair (C. C. A. 2) 121 Fed. 2d, 945, 947-948.

Commissioner vs. Marshall (C. C. A. 2) 125 Fed. 2d, 943, 946-947.

Under the provisions of Section 510 of the gift tax statute, it is axiomatic that a taxable gift *inter vivos* must be a complete bilateral transaction involving a transfer to a determinable donee. It seems impossible to believe that Congress intended to impose a gift tax and impress liability therefor upon the presumptive donee where the interest of such donee is wholly dependent, as a condition precedent, upon the mere whim or

fancy of a human being. *Porter vs. Commissioner* (C. C. A. 2) 60 Fed. 2nd, 673, 674; Affm'd 289 U. S. 436. As stated in cases above cited:

> "A gift is a bilateral transaction and demands a donee as well as a donor; it is incomplete though the donor has parted with his interest, if the donee remains indeterminate, and the beneficiaries are determined only when the power to change them ends."

Hesslein vs. Hoey (C. C. A. 2) 91 Fed. 2d, 954, 956; Certiorari denied, 302 U. S. 756.

Sanford's Estate vs. Commissioner, 308 U. S. 39, 46.

Helvering vs. Blair (C. C. A. 2) 121 Fed. 2d, 945, 947-948.

The decision of the Court below therefore appears to have decided an important question of law as to the interpretation of the gift tax statute, which should be finally settled beyond question by this Court.

An article on "Taxes on Gifts Subject to Contingencies" by Walter L. Nossaman is scheduled for appearance in the coming October issue of the magazine "Taxes." It contains a critical review of decisions of the Circuit Court for the Second Circuit in the *Marshall* and *Herzog* cases, and also on the present case of *Smith vs. Shaughnessy*, as related to the decision of the Supreme Court in the *Sanford* case. Without quoting from the body of said article, we repeat the conclusion reached therein as follows:

> "The present problem has reached a stage where the need of legislative or judicial solution is urgent. The result of the recent decisions dealing with it is, the pres-

ent writer believes, as impractical as it is unjust. It is to be hoped that the circuits in which the problem has not arisen will apply a more critical and realistic view than that applied in the *Marshall* case. The way would then be opened—perhaps it is open now—for a hearing in the Supreme Court which would finally resolve the issue. It seems improbable in the extreme that the court which decided *Sanford's Estate v. Commissioner* would follow the rule laid down in *Commissioner v. Marshall*, or *Smith v. Shaughnessy*."

In the July, 1942, issue of "Estate Conservation," a publication prepared and edited by the Alexander Publishing Company, appears an article entitled "Retaining an Interest in Trust Property—Double Taxation," from which we quote the following:

> "One of the most confused questions in the tax law may be illustrated by these simple facts: John Doe creates a trust the income from which is to be paid to his wife, Mary Doe, for life and upon her death the trust property is to be distributed to his two children, James Doe and John Doe. In the event, however, the children predecease his wife, the property is to be returned to him, if living.
>
> Is the transfer of the property to such a trust subject to a gift tax, to an estate tax or both? If both, what property measures each tax?
>
> When a trust is created the first tax problem in point of time is whether the transfer is subject to a gift tax? The answer to this question depends upon whether a completed gift has been made. As was said in a recent decision, 'It might have been logical for Congress in the gift tax provisions to describe with particularity

those factors determinative of the question whether a completed gift has been made. However, as Congress has not done so we must seek an answer in the decisions of the courts.

The United States Supreme Court had said in the *Sanford's* estate that there is nothing in the language of the statute to suggest that Congress intended to tax gifts before the donor had fully parted with his interest in the property given or that the test of completeness of the taxed gift is any different from that to be applied in determining whether the donor has retained such an interest as becomes subject to an estate tax upon its extinguishment by death. The gift tax is supplementary to the estate tax and both are to be construed together. However, the two taxes are not always mutually exclusive. Gifts in contemplation of death, for example, which are complete and taxable when made are also required to be included in the gross estate for purposes of taxation. If the statutes are not mutually exclusive the question naturally arises in what cases do they overlap?

* * * * * * * *

In the meantime the courts have held that where there is a trust with a possibility of reverter that there is a gift tax measured by the property transferred; that there is a gift measured only by the value of the life estate; that there is an estate tax measured by the full value of the property transferred; that there is an estate tax measured by the value of the remainder interest.

Until the Supreme Court has clarified this confusion, taxpayers should file refund claims if full Gift and Estate Taxes have been paid."

CONCLUSION

It is therefore respectfully submitted that this petition for writ of certiorari to review the judgment of the Circuit Court of Appeals for the Second Circuit should be granted.

Dated September 21, 1942.

GEORGE R. FEARON,
Attorney for Petitioner.

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821 Onondaga Co. Sav. Bk. Bldg.,
Syracuse, New York.

APPENDIX

Revenue Act of 1932:

SEC. 501. IMPOSITION OF TAX.

(a) For the calendar year 1932 and each calendar year thereafter a tax, computed as provided in Section 502, shall be imposed upon the transfer during such calendar year by any individual, resident or non-resident, of property by gift.

(b) The tax shall apply whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property is real or personal, tangible or intangible; * * * (Internal Rev. Code, Sec. 1000).

SEC. 510. LIEN FOR TAX.

The tax imposed by this title shall be a lien upon all gifts made during the calendar year, for 10 years from the time the gifts are made. If the tax is not paid when due, the donee of any gift shall be personally liable for such tax to the extent of the value of such gift. * * * (Internal Rev. Code, Sec. 1009.)

Treasury Regulations 80 (1937 ed.):

ART. 24 (in part). Ordinarily a general power is one to appoint to any person or persons in the discretion of the donee of the power, or, however limited as to the persons or objects in whose favor the appointment may be made, is exercisable in favor of the donee, his estate or his creditors.

New York Real Property Law. Sec. 184:

SEC. 184. *General Power.* A power is general where it authorizes the transfer or incumbrance of a fee, by either a conveyance or a will of, or a charge on, the property embraced in the power, to any grantee whatever.

New York General Construction Law. Sec. 37 (in part):

SEC. 37. *Person.* The term person includes a corporation and a joint-stock association.

FILE COPY

Office - Supreme Court, U. S.
FILED
JAN 7 1943
CHARLES ELMORE CROPLEY
CLERK

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1942

No. 429

HURLBUT W. SMITH,

Petitioner,

vs.

FRANK J. SHAUGHNESSY, COLLECTOR OF INTERNAL REVENUE OF THE UNITED STATES FOR THE TWENTY-FIRST DISTRICT OF NEW YORK.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit

BRIEF FOR PETITIONER

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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1942

No. 429

HURLBUT W. SMITH,

Petitioner,

vs.

FRANK J. SHAUGHNESSY, COLLECTOR OF INTERNAL REVENUE OF THE UNITED STATES FOR THE TWENTY-FIRST DISTRICT OF NEW YORK.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit

BRIEF FOR PETITIONER

Opinions Below

The opinion of the District Court (R. 25-28) is reported at 40 F. Supp. 19. The Per Curiam opinion of the Circuit Court of Appeals (R. 37) is reported at 128 F. (2d) 742.

Jurisdiction

The judgment of the Circuit Court of Appeals was entered on July 6, 1942 (R. 37). The Petition for Certiorari

was filed on September 29, 1942, and granted on November 9, 1942. (R. 38) The jurisdiction of this court is conferred by section 240(a) of the Judicial Code, as amended. (28 U. S. C. A. §347)

Question Presented

In 1937 the petitioner, as grantor, transferred securities in trust, the income from which was payable to his wife for life, and, upon her death, the principal was payable to the grantor, if living, and if not living then to such persons as the wife might by will appoint, or, in default of such testamentary disposition, then to her intestate successors. Is the grantor subject to gift tax upon anything other than the value of the life estate?

Statutes and Regulations Involved

The statutes involved are set forth in the Appendix, *infra*, p. 16.

Statement

The case was tried without a jury. (R. 1, 41) The District Court made findings of fact and conclusions of law. (R. 29-32)

On February 26, 1937, the petitioner, as grantor, pursuant to a trust indenture (R. 6-10) transferred to The Syracuse Trust Company 3,000 shares of convertible preferred stock of L. C. Smith & Corona Typewriters, Inc., in trust. The trustee was directed to pay over the net income from the fund quarterly to Gladys D. Smith, wife of the grantor, during her life and, upon her death, to pay over the principal of the trust to the grantor if he be then living. In the event the grantor predeceased the life beneficiary, then the trustee was directed upon her death to pay over the principal of the trust to such person or persons as she should by her will direct. In the event of the failure of the life beneficiary to make testamentary disposition of the

fund, then the trustee was directed to pay the same over to such person or persons as would take under the laws of New York, had the principal of the fund been owned outright by her and she had died intestate. (R. 29-30)

The value of the entire principal of the fund on the date of the creation of the trust was $570,937.50. (R. 31) On March 15, 1938, the petitioner filed a gift tax return in which he reported the full value of the principal of the trust fund. After deducting therefrom the exemption of $40,000 and the $5,000 exclusion, the Collector assessed a gift tax of $71,674.22 which the petitioner thereon paid. (R. 30) Three days later the petitioner filed a claim for the refund of the total amount of tax paid on the ground that the transfer in trust did not constitute a taxable gift. (R. 30) Upon rejection of that claim, this action was commenced. (R. 30-31)

On the date of the creation of the trust the value of the life interest of Gladys D. Smith was $322,433.53. (R. 31). No finding was made with respect to the value of the grantor's reversionary interest or of the interests of the possible remaindermen. The District Court held that the value of the life estate was subject to gift tax in the amount of $31,565.03. (R. 32) The court further held that the petitioner was not subject to gift tax upon anything other than the value of the life estate, and entered judgment in his favor for $40,109.19, being the balance of the tax paid on the return. (R. 32-33)

Upon the Government's appeal, it was contended that the District Court erred in not holding that the entire value of the securities transferred in trust, less only the value of the grantor's reversionary interest,[1] was subject to gift

[1] The Government's brief in the Circuit Court of Appeals contained the following note:

"The Bureau of Internal Revenue has advised that by actuarial computation, the value of the retained interest of the grantor in the instant case is $49,191.975 ($0.08616×$570,937.50)." [Br., p. 7]

tax. (R. 35) In a Per Curiam opinion, the Circuit Court of Appeals reversed on the authority of *Herzog* v. *Commissioner*, 116 F. (2d) 591 (C. C. A. 2d). (R. 37). The effect of the decision below is to impose a gift tax upon the entire value of the securities transferred in trust. The case is here on certiorari. (R. 38)

Specification of the Error to Be Urged

The Circuit Court of Appeals erred in holding that a gift tax was payable with respect to all or any part of the corpus of the trust fund.

Summary of Argument

The gift tax was imposed as a supplement to the estate tax, to tax transfers of property beyond the reach of the estate tax. The two taxes must be correlated. Correlation requires the application of one test: If the property interest is subject to the estate tax, then it is not subject to the gift tax. In other words, if the transfer *inter vivos* was "incomplete" for estate tax purposes, then the property interest is included in the gross estate and subject to the estate tax; and the gift tax does not apply. On the other hand, if the transfer of the property interest was "completed" *inter vivos*, then the gift tax is imposed and the estate tax does not apply.

If this reasonably simple test is applied, there will be no "overlapping"—except where Congress has specifically (and appropriately) provided for the imposition of both taxes. Instances of "overlapping" should be extended only by the Congress.

By the transfer in trust in 1937 the petitioner retained a reversionary interest which was prior in point of time to the ultimate disposition of the trust corpus, and which interest was terminable only by his death. The transfer was,

therefore, one intended to take effect in possession or enjoyment at or after his death, and the value of the corpus will be includible in the petitioner's gross estate at his death. The transfer was "incomplete" for estate tax purposes; and the gift tax does not apply.

Argument

(1) There was no completed gift of any part of the corpus of the Trust

Under *Helvering* v. *Hallock*, 309 U. S. 106, it is clear that upon the death of the grantor the then value of the corpus of this trust (less the value of the life estate)[2] will be includible in the decedent's gross estate for federal estate tax purposes as a transfer "intended to take effect in possession or enjoyment at or after death". (Sec. 811(c), I. R. C.) The reason for this result is that under the trust indenture the grantor has a reversionary interest similar to those in the *Hallock* case, *supra*, which, unless relinquished during his life, is terminable only by his death prior to that of the life tenant.

The question here is, to what extent a transfer subject to estate taxation at death by virtue of that which the decedent "retained" during his life is also subject to gift taxation at the time of the *inter vivos* transfer? Rephrased, the question is, whether *inter vivos* gifts of the type held "incomplete" in the *Hallock* case, for federal estate tax purposes, constitute "completed" gifts for federal gift tax purposes?

In *Estate of Sanford* v. *Commissioner*, 308 U. S. 39, this Court held that an *inter vivos* transfer of property was incomplete for gift tax purposes, where the donor reserved to

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[2] In its petition for certiorari in the *Hallock* case, the Government conceded that the value of the life interests was not a part of the gross estate. See *Central National Bank of Cleveland* v. *United States*, 94 Ct. Cl. 527, 544-545; 41 F. Supp. 239; *Estate of Horatio Gates Lloyd*, 47 B. T. A. 349, 357.

himself power to designate new beneficiaries other than himself.[3] Prior to that decision, this Court had held in *Porter* v. *Commissioner*, 288 U. S. 436, that the relinquishment of such a reserved power at death was a taxable transfer for estate tax purposes.

In deciding the *Sanford* case, this Court said:

> "We are concerned here with a question to which Congress has given no answer in the words of the statute, and it must be decided in conformity to the course of judicial decision applicable to a unified scheme of taxation of gifts whether made *inter vivos* or at death. * * *" [P. 48]
>
> "There is nothing in the language of the statute, and our attention has not been directed to anything in its legislative history to suggest that Congress had any purpose to tax gifts before the donor had fully parted with his interest in the property given, or that the test of the completeness of the taxed gift was to be any different from that to be applied in determining whether the donor has retained an interest such that it becomes subject to the estate tax upon its extinguishment at death. The gift tax was supplementary to the estate tax. The two are in *pari materia* and must be construed together. *Burnet v. Guggenheim, supra*, 286. An important, if not the main, purpose of the gift tax was to prevent or compensate for avoidance of death taxes by taxing the gifts of property *inter vivos* which, but for the gifts, would be subject in its original or converted form to the tax laid upon transfers at death." [P. 44] [4]

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[3] The Government was so uncertain concerning that issue that it took inconsistent positions and even argued both sides of the question in this Court. (Cf., *Rasquin* v. *Humphreys*, 308 U. S. 54.)

[4] The Court's conclusion is fully supported by its references to the legislative history of the gift tax provisions of the Revenue Acts of 1924 and 1932, which references read as follows:

> "The gift tax provisions to the Revenue Act of 1924 were added by amendments to the revenue bill introduced on the floor of the House and the Senate. Cong. Rec., Vol. 65, Part 3, pp. 3118-3119; Part

In view of the fact that, under the *Hallock* case, the value of the remainder interests in the instant case will be includible in the petitioner's gross estate for estate tax purposes, it is self-evident that under the "test of completeness" applied in the *Sanford* case the gift is incomplete for gift tax purposes.

The above-quoted language was applied in a case where the grantor reserved the power to designate new beneficiaries other than himself. We submit that the whole rationale of the *Sanford* case is equally applicable to the instant case where the grantor reserved the reversionary right to the entire corpus. In both, either death or a further *inter vivos* relinquishment of the reserved right is necessary before the grantor will have parted fully with the corpus. In both, the relinquishment at death will subject the value of the corpus to estate tax.

4, pp. 3170, 3171; Part 8, p. 8094. The sponsor of the amendment in both houses urged the adoption of the bill as a 'corollary' or as 'supplemental' to the estate tax. Cong. Rec., Vol. 65, Part 3, pp. 3119-3120, 3122; Part 4, p. 3172; Cong. Rec., Vol. 65, Part 8, pp. 8095, 8096.

"The gift tax of 1924 was repealed when Congress, concurrently with the enactment of § 302(c) of the Revenue Act of 1926, 44 Stat. 70, 125, 126, establishing a conclusive presumption that gifts within two years of death were made in contemplation of death and therefore subject to the estate tax. A gift tax was reenacted by § 501 of the Revenue Act of 1932, 47 Stat. 169, shortly after it was decided in *Heiner* v. *Donnan*, 285 U. S. 312, that the legislative enactment of such a presumption violated the Fifth Amendment." [308 U. S. 44, N. 1]

See also, S. Rept. 665, 72d Cong., 1st Sess. (1932) 40, wherein the gift tax provisions of the Revenue Act of 1932 are referred to as "an adjunct of the estate tax". With further reference to the purpose of the gift tax, the Report contains the following statement: "In short, the design is to impose a tax which measurably approaches the estate tax which would have been payable on the donor's death had the gifts not been made and the property given had constituted his estate at his death. The tax will reach gifts not reached, for one reason or another, by the estate tax." The Report of the Ways and Means Committee of the House contains identical statements (H. Rept. 708, 72d Cong., 1st Sess. (1932) 28-29).

In the *Sanford* case there was no possibility that the grantor would ever personally enjoy either the income or the corpus. In the instant case there is a possibility that the corpus will revert to the grantor. Indeed, the death of the life tenant prior to that of the grantor will alter the entire flow of benefits under the trust. However, distinctions of this kind between the particular type of right retained by a grantor, based upon the quantum of the reserved right or the economic control exercisable, only lead into the sophistries of property law rejected as unimportant in the *Hallock* case. Thus, in that case this Court, quoting from the dissent in *Helvering* v. *St. Louis Union Trust Co.*, 296 U. S. 39, said:

> "'Having in mind,' said the dissenters, 'the purpose of the statute and the breadth of its language it would seem to be of no consequence what particular conveyancers' device—what particular string—the decedent selected to hold in suspense the ultimate disposition of his property until the moment of his death. In determining whether a taxable transfer becomes complete only at death we look to substance, not to form . . . . *However we label the device it is but a means by which the gift is rendered incomplete until the donor's death.*' 296 U. S. at 47, 80 L. Ed. 34, 56 S. Ct. 74, 100 A. L. R. 1239. * * *" [P. 114—Italics ours]

The application of the *Sanford* case and the *Hallock* case to the present transfer is obvious. Here the grantor at the time of the creation of the trust made an unqualified gift of a life estate to his wife. The grantor has no power during his life to alter the enjoyment of that estate. It will be unaffected by his death. A completed gift of the life estate was, therefore, made which is admittedly subject to the gift tax. However, until the death of the grantor, or the prior relinquishment of his reversionary interest, the possession and enjoyment of the remainder interests are suspended.

No one can determine whether any actual gift of these interests has been made until the death of either the grantor or the life tenant. The remainder interests being thus subject to the reversionary right of the grantor were, as of the date of the creation of the trust, incomplete and, if not rendered complete until the death of the grantor, will then be included as a part of his estate for estate tax purposes. It follows that there was no complete gift of the remainders and, as to these, the gift tax is not applicable.

(2) The doctrine of the *Sanford* case should not be restricted to transfers in trust where the grantor reserved the power to change the beneficiaries.

After the decision of this Court in the *Hallock* case, The Tax Court of the United States consistently ruled that under the *Sanford* case there was no completed *inter vivos* gift where, as here, the grantor of a trust retained a reversionary interest contingent upon survival of the life tenant.[5]

Various circuit courts of appeal have reached a different result.[6]

The case of *Commissioner* v. *Marshall*, 125 F. (2d) 943 (C. C. A. 2d), is typical. There the Court attempted to distinguish the *Sanford* case, and to limit its application to cases where the grantor of a trust reserved "power to alter the flow of benefits" [P. 949]. It concluded that the value of contingent remainders is subject to gift tax, even though they will also be subject to estate tax. In reaching this

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[5] *Margaret White Marshall*, 43 B. T. A. 99; *Carl J. Schmidlapp*, 43 B. T. A. 829, 837-838; *William J. McCormack*, 43 B. T. A. 924, 929; *Morris Michel*, 43 B. T. A. 1036, 1038-1039.

[6] *Commissioner* v. *Marshall*, 125 F. (2d) 943 (C. C. A. 2d); *Commissioner* v. *McLean*, 127 F. (2d) 942 (C. C. A. 5th); *Helvering* v. *Robinette*, 129 F. (2d) 832 (C. C. A. 3d); Cf., *Herzog* v. *Commissioner*, 116 F. (2d) 591 (C. C. A. 2d).

result, the Court pointed to the fact that in certain instances gift and estate taxes necessarily overlap, and reasoned that because of this the *Sanford* case did not forbid the imposition of both gift and estate taxes upon a transfer where, as here, the grantor reserved a reversionary interest in the corpus of the trust.

The estate tax law contains a provision allowing a credit with respect to transfers previously subjected to the gift tax (Sec. 813 (a), I. R. C.). After referring to that provision, this Court in the *Sanford* case said:

> "The two taxes are thus not always mutually exclusive as in the case of gifts made in contemplation of death which are complete and taxable when made, and are also required to be included in the gross estate for purposes of the death tax. But § 322 is without application unless there is a gift *inter vivos* which is taxable independently of any requirement that it shall be included in the gross estate. * * *" [P. 45]

Obviously, this Court did not refer to gifts in contemplation of death as being the only ones with respect to which there might be both a gift and estate tax upon the same transfer.

To the extent that Congress expressly directs, there may, of course, be double taxation. (*Hellmich* v. *Hellman*, 276 U. S. 233) Thus, this Court in *Helvering* v. *Bullard*, 303 U. S. 297, upheld the imposition of an estate tax on an irrevocable transfer of a vested remainder subject to a life estate in the donor. Such a transfer would seem to be a completed gift. However, in the absence of a specific direction by Congress in the Joint Resolution of March 3, 1931 (46 Stat. 1516), such a transfer would not have been subject to the estate tax. (*May* v. *Heiner*, 281 U. S. 238)[7]

[7] In its brief in opposition (p. 9), the government suggested that gift and estate taxes overlap in the case of tenancies by the entirety. Congress has expressly directed that such tenancies shall be subject to the estate tax.

The difficulty with the reasoning of the courts in *Commissioner* v. *Marshall, supra*, and other similar cases is that the instances of overlapping relied upon were of statutory creation, wherein the estate tax—for the purpose of minimizing *inter vivos* tax avoidance transfers— was extended into the otherwise exclusive field of a gift tax. Cf. *Helvering* v. *City Bank Farmers Trust Co.*, 296 U. S. 85. This statutory extension of the estate tax, however, does not support a like judicial extension of the gift tax into the field of the estate tax. The *Sanford* case recognizes the former, but forbids the latter. Nor is the provision in the estate tax law for a credit with respect to transfers previously subjected to the gift tax support for any such extension. (Sec. 813 (a), I. R. C.) The credit is the result of the statutory overlap of the estate tax into the gift tax—not the reason for it. It does not justify extending the gift tax by judicial decision to *inter vivos* transfers held by this Court to be incomplete for estate tax purposes.

It is certainly too clear for further argument that the rationale of the *Sanford* case is logically applicable to transfers where, as here, the grantor has reserved a reversionary interest sufficient to subject the contingent remainders to the estate tax. To limit that doctrine to the bare facts involved in the *Sanford* case, as suggested by the Court in *Commissioner* v. *Marshall, supra*, will destroy the correlation between the gift and estate taxes, and will necessarily extend the gift tax into the estate tax field already covered by the *Hallock* case.

The adoption of the Government's contention here will

(Sec. 811(3), I. R. C.) The extent to which the gift tax also applies has not yet been finally determined. The Tax Court of the United States has held that the creation of a tenancy by the entirety does not result in a taxable gift. (*William H. Hart*, 36 B. T. A. 1207) Two circuit courts of appeal have held otherwise. (*Lilly* v. *Smith*, 96 F. (2d) 341 (C. C. A. 7th); *Commissioner* v. *Hart*, 106 F. (2d) 869 (C. C. A. 3d)) If any overlap exists, it is because of the specific provisions of the estate tax law.

produce highly undesirable results from the standpoint of sound administration. It would result in double taxation, which this Court has said is never presumed. (*Moss* v. *Higgins*, 312 U. S. 443, 449) Furthermore, as a general principle, it would subject contingent donees to a secondary gift tax liability on property which they might never receive. The statute provides that the gift tax shall be paid by the donor (Sec. 1008 (a), I. R. C.), that it shall be a lien upon all property transferred, and that personal liability for payment extends to the donee. (Sec. 1009, I. R. C.) After referring to these provisions, this Court in *Burnet* v. *Guggenheim*, 288 U. S. 280, said:

> "A statute will be construed in such a way as to avoid unnecessary hardship when its meaning is uncertain. [Citing cases] Hardship there plainly is in exacting the immediate payment of a tax upon the value of the principal when nothing has been done to give assurance that any part of the principal will ever go to the donee. The statute is not aimed at every transfer of the legal title without consideration. Such a transfer there would be if the trustees were to hold for the use of the grantor. It is aimed at transfers of the title that have the quality of a gift, and a gift is not consummate until put beyond recall." [Pp. 285-286]

Finally, the adoption of the Government's contention here would necessitate resort, for gift tax purposes, to a wholly unrealistic valuation of remainder interests. (See *Commissioner* v. *McLean*, 120 F. (2d) 942 (C. C. A. 5th).) The trust device lends itself to the use of an infinite variety of contingencies, the happening of which may not only depend upon the prior death of a beneficiary or the grantor, but also upon the possibility of marriage, of future birth, etc. (See *Helvering* v. *Robinette*, 129 F. (2d) 832 (C. C. A. 3d).) The Circuit Court of Appeals in *Commissioner* v. *Marshall*, *supra*, approved the use of mortality

tables in a situation where only comparative life expectancies were involved. Even this was an extension of the use of such tables, not to measure the value of what the donor actually had received, but to measure the value of what he might never receive. (See, also, *Meierhof* v. *Higgins*, 129 F. (2d) 1002 (C. C. A. 2d).) Complicate the situation by the existence of a contingency based upon the possibility of marriage, and the problem becomes insurmountable. (See *Humes* v. *United States*, 276 U. S. 487.)

The rule of the *Sanford* case avoids these difficulties. Furthermore, it is comparatively simple to apply. The whole approach is from the standpoint of the estate tax. If the transfer is includible in the gross estate, there is no gift tax liability except where Congress has specifically created an overlap in the two taxes. The scope of the gift tax is thus clearly defined. Any broadening of this scope is a matter for the Congress.

The case of *Herzog* v. *Commissioner*, 116 F. (2d) 591 (C. C. A. 2d), on the authority of which the court below reversed the judgment of the District Court in the instant case (R. 37), is clearly distinguishable. There the grantor made a complete *inter vivos* disposition of the trust property without reserving any right other than a mere passive expectancy that the trustee might in his discretion distribute the trust income to him. As the court pointed out (p. 595), the trust corpus would not be includible in the gross estate of the grantor at his death. The imposition of the gift tax was, therefore, entirely consistent with the decision of this court in the *Sanford* case.

Conclusion

The petitioner made no completed gift of any part of the corpus of the trust in 1937. He is not, therefore, subject to gift tax upon anything other than the value of the life

estate. The judgment of the Circuit Court of Appeals is erroneous and should be reversed. The judgment of the District Court should be affirmed. If, contrary to the argument herein, this court concludes that the petitioner is subject to gift tax upon anything other than the value of the life estate, then, as conceded by the government in the court below, the value of the petitioner's reversionary interest should be excluded and the case should be remanded for the purpose of determining the value of that interest.

Respectfully submitted,

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APPENDIX

"Revenue Act of 1932, c. 209, 47 Stat. 169:

"SEC. 501. IMPOSITION OF TAX.

"(a) For the calendar year 1932 and each calendar year thereafter a tax, computed as provided in section 502, shall be imposed upon the transfer during such calendar year by any individual, resident or nonresident, of property by gift.

"(b) The tax shall apply whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property is real or personal, tangible or intangible: * * *"

"SEC. 506. GIFTS MADE IN PROPERTY.

"If the gift is made in property, the value thereof at the date of the gift shall be considered the amount of the gift."

"SEC. 509. PAYMENT OF TAX.

"(a) TIME OF PAYMENT.—The tax imposed by this title shall be paid by the donor * * *"

"SEC. 510. LIEN FOR TAX.

"The tax imposed by this title shall be a lien upon all gifts made during the calendar year, for ten years from the time the gifts are made. If the tax is not paid when due, the donee of any gift shall be personally liable for such tax to the extent of the value of such gift. * * *"

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No. 429

In the Supreme Court of the United States

OCTOBER TERM, 1942

HURLBUT W. SMITH, PETITIONER

v.

FRANK J. SHAUGHNESSY, COLLECTOR OF INTERNAL REVENUE OF THE UNITED STATES FOR THE TWENTY-FIRST DISTRICT OF NEW YORK

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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OPINIONS BELOW

The opinion of the District Court (R. 36) is reported in 40 F. Supp. 19. The opinion of the Circuit Court of Appeals (R. 57) is reported in 128 F. (2d) 742.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on July 6, 1942 (R. 58-59). The petition for a writ of certiorari was filed September 29, 1942. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the grantor of a trust of securities, under which the income is to be paid to the grantor's wife for life and upon her death the principal is to be paid to him if living, and, if he should not then be living, to her legatees or, if she should die intestate, to her intestate successors, is subject to gift tax under Sections 501 and 506 of the Revenue Act of 1932.

STATUTE AND REGULATIONS INVOLVED

The statute and regulations involved are set forth in the Appendix, *infra*, pp. 11 *et seq.*

STATEMENT

On February 26, 1937, the taxpayer created an irrevocable trust the corpus of which consisted of securities valued at $570,937.50. The trust indenture provided that the income should be paid to his wife for life, and upon her death the principal to be paid to him if living, or in the event of his prior death, the principal to be paid to the persons and in the amounts directed in her will, but if she should die intestate, the principal to be paid to the persons and in the amounts provided under New York law as though she had owned outright the corpus of the trust and had died intestate (R. 42–43, 44).

In his gift tax return for 1937 the taxpayer reported the full amount of $570,937.50 as a taxable gift, and paid a tax of $71,674.22 thereon.

Thereafter, the taxpayer filed a claim for refund of the tax on the ground that the transfer did not constitute a taxable gift. The Commissioner rejected the claim and the taxpayer thereupon brought suit in the District Court (R. 43–44).

The District Court held that the transfer in trust constituted a complete and absolute gift only to the extent of the life estate in the taxpayer's wife (R. 45), and accordingly on September 9, 1941, entered judgment of refund to the taxpayer in the amount of $40,109.19 (R. 46–47). The taxpayer did not appeal from the District Court's decision that the value of the life estate was subject to gift tax. On the Commissioner's appeal the Circuit Court of Appeals in a memorandum opinion reversed the judgment of the District Court and remanded the cause with direction to dismiss the complaint, on the authority of its decision in *Herzog* v. *Commissioner*, 116 F. (2d) 591 (R. 57–59).

ARGUMENT

The taxpayer contends that the decision below is apparently in conflict with the decisions of this Court in *Estate of Sanford* v. *Commissioner*, 308 U. S. 39, and *Helvering* v. *Hallock*, 309 U. S. 106. The contention seems to be based on the following arguments: (1) Under the *Sanford* case a gift tax cannot be imposed unless the *inter vivos* transfer is complete, and the transfer in the present case is not complete; (2) in any event since under the *Hal-*

lock case the corpus of the instant trust will be included in the grantor's estate and will be taxed as such, the grantor cannot now be subjected to a gift tax. No conflict among the circuits is asserted. Indeed, petitioner's arguments have been uniformly rejected by the circuit courts of appeals. *Commissioner* v. *Marshall*, 125 F. (2d) 943 (C. C. A. 2d); *Commissioner* v. *McLean*, 127 F. (2d) 942 (C. C. A. 5th); *Helvering* v. *Robinette*, 129 F. (2d) 832 (C. C. A. 3d); *Herzog* v. *Commissioner*, 116 F. (2d) 591 (C. C. A. 2d); cf. *Higgins* v. *Commissioner*, 129 F. (2d) 237 (C. C. A. 1st); *Commissioner* v. *Beck's Estate*, 129 F. (2d) 243 (C. C. A. 2d), and *Hughes* v. *Commissioner*, 104 F. (2d) 144 (C. C. A. 9th).

(1) In *Estate of Sanford* v. *Commissioner*, 308 U. S. 39, and *Rasquin* v. *Humphreys*, 308 U. S. 54, this Court held that the grantor of an *inter vivos* trust who reserves the power to designate new beneficiaries other than himself, is subject to a gift tax at the time he relinquishes that power but not before then. Those cases are premised on the proposition that a transfer by which the transferor retains the power to alter the transferees is so incomplete that it does not constitute a gift. Petitioner seeks to expand those decisions to make them applicable to a transfer by which the grantor parts completely with control over the property, and its distribution, but reserves a contingent reversionary

interest. The circuit courts have without exception dismissed attempts of this sort.

The petitioner's argument overlooks the distinction between a grantor's retention of a continuing power to alter the distribution of the property and his retention of a contingent interest, the fruition of which depends upon events wholly beyond his control. Where the grantor retains the power to shift the enjoyment of the fund, even though he is excluded as a possible beneficiary of that power, the absence of a complete donation is at once apparent, for the grantor has retained one of the most significant fagots of the bundle of rights constituting ownership, *viz.*, the right to dispose of the property. Stated another way, the grantor in such a case retains control over the economic benefits of the property. In that circumstance the reason for the nonapplication of the gift tax becomes at once apparent. The gift is not effected until the relinquishment of the power because until that time the *sine qua non* of a complete donation, *viz.*, the surrender of the grantor's control over the economic benefits of the property, does not take place. However, the grantor in this case retained no control over the economic benefits of the property. *Commissioner* v. *Marshall*, *supra*. It is this control or "'command over the property taxed'" which was said in the *Sanford* case to be the essence of the taxable gift. And the relinquishment of this control makes the gift taxable.

In urging that the transfer is at present incomplete the petitioner also emphasizes the indefiniteness of the identity of the ultimate donees. Relying upon the provision of the trust that the wife may dispose of the trust estate by her will, he argues that where the remaindermen are so indeterminable there can be no completed gift of the entire estate. A taxable gift *inter vivos* must, he contends, be a complete bilateral transaction involving a transfer to a determinable donee. Reliance is placed (Pet. 10) on language appearing in the decisions of the Second Circuit in *Porter* v. *Commissioner*, 60 F. (2d) 673, 674, affirmed, 288 U. S. 436, and *Hesslein* v. *Hoey*, 91 F. (2d) 954, 956, certiorari denied, 302 U. S. 756. However, in its later decision in *Herzog* v. *Commissioner*, *supra*, p. 595, the Second Circuit said that the language of its earlier decisions, relied on by the taxpayer here, was used only in respect to a power reserved to the grantor and, inferentially, was not applicable to a situation where the grantor had parted with all control over the appointment. Similarly, the *Sanford* case, *supra*, p. 46, which the taxpayer cites at this point (Pet. 10) was addressed, as the succeeding language (pp. 46–47) shows, to the situation in which the *grantor* retains the power to alter the donee. The statement in that case on which the taxpayer relies was merely that Congress could not have intended to impose personal liability upon the donee of a gift of property, so incomplete

that he might be deprived of it *by the donor* the day after he had paid the tax.

The same contention was discussed and rejected in *Herzog* v. *Commissioner*, *supra*, pp. 594–595, and *Helvering* v. *Robinette*, *supra*, pp. 834, 835–836. The test of the incidence of the gift tax is whether the *donor* has completely parted with control over the property. The language of the statute and Article 3 of the Regulations makes it plain that the taxable event is not the absolute vesting of rights in *particular* beneficiaries but the irrevocable divestment of the donor's rights in the property. The argument (Pet. 9–10) that the interests of the remaindermen are wholly dependent upon the mere whim or fancy of a human being would have merit if the whim were that of the grantor. But here the grantor has placed the property beyond his control. Whether he or any particular person will enjoy it is a matter beyond his power to determine.

2. Petitioner's second contention—that the possibility that under the *Hallock* case the corpus of the instant trust will ultimately be included in the petitioner's gross estate precludes the applicability of a gift tax now—is also not borne out by the decisions.

At the very outset, it should be observed that the statute contemplates a certain amount of overlapping between the gift and estate tax provisions, and indeed specifies that the gift tax shall be credited

against the estate tax to the extent that the same property is included in the gross estate.[1]

As an initial matter, the unglossed text of Sections 501 (a) and (b) and 506 of the Revenue Act of 1932 (Appendix, *infra*), the provisions of Articles 2, 3, 17 and 19 of Treasury Regulations 79 (1936 ed.) (Appendix, *infra*), and the legislative history of the gift tax provisions,[2] all establish that the interests here created are subject to the gift tax. Cf. *Commissioner* v. *Beck's Estate*, *supra*, p. 244; *Commissioner* v. *Marshall*, *supra*, p. 945. For gift tax purposes there may be immediate gifts of future interests, whether vested or contingent. *Helvering* v. *Hutchings*, 312 U. S. 393; *United States* v. *Pelzer*, 312 U. S. 399; *Ryerson* v. *United States*, 312 U. S. 405; *Commissioner* v. *Marshall*, *supra*, p. 945; *Helvering* v. *Blair*, 121 F. (2d) 945 (C. C. A. 2d). But the petitioner contends that the doctrines of the *Hallock* and *Sanford* cases, *supra*, must be read as a gloss upon the generality of the provisions imposing the gift tax. It is clear that although the *Sanford* case discusses the correlation between the gift and estate taxes, it does not suggest that the ultimate imposition of the latter precludes the incidence of the former. On the contrary, the case contains an explicit indication that

[1] Section 802, Revenue Act of 1932, c. 209, 47 Stat. 169, as amended by H. J. Res. 60, March 17, 1941, c. 21, 55 Stat. 44.

[2] H. Rep. No. 708, 72d Cong., 1st Sess., p. 27 (1939–1 Cum. Bull., Part 2, 457, 476–477); S. Rep. No. 665, 72d Cong., 1st Sess., p. 39 (1939–1 Cum. Bull. (Part 2), 496, 524–525).

the two taxes are not mutually exclusive. 308 U. S. at 45. And in *Herzog* v. *Commissioner, supra, Commissioner* v. *Marshall, supra,* and *Helvering* v. *Robinette, supra,* the courts approved a gift tax on a transfer such as is here involved notwithstanding the recognized possibility that an estate tax would also be imposed. See also *Higgins* v. *Commissioner, supra.* Nor does the *Hallock* case, which dealt solely with estate taxes, contain any intimation as to the incidence of gift taxes.

Moreover, instances of overlapping are frequently found in the decided cases. Thus, a vested remainder after a retained life estate in the donor is subject to the estate tax. *Helvering* v. *Bullard,* 303 U. S. 297. Yet it is inconceivable that the gift tax would not also attach at the time that the remainder was created. Again, the overlapping of the two taxes is shown in the case of a tenancy by the entirety. *Tyler* v. *United States,* 281 U. S. 497; *Helvering* v. *Bowers,* 303 U. S. 618; *Lilly* v. *Smith,* 96 F. (2d) 341 (C. C. A. 7th), certiorari denied, 305 U. S. 604; *Commissioner* v. *Hart,* 106 F. (2d) 269 (C. C. A. 3d). The taxpayer's contention necessarily assumes that the *Sanford* case has inferentially overruled the foregoing decisions, an assumption that is unwarranted by the opinion.

In the court below the Collector conceded that the value of the grantor's reversionary interest should be deducted from the entire value of the securities transferred in trust. (R. 53; Pet. 7.)

However, the effect of the decision below was to tax the entire value of the trust estate without such reduction. Although this result does not accord with *Commissioner* v. *McLean*, 127 F. (2d) 942 (C. C. A. 5th), the taxpayer nevertheless does not appear to have made a point of this aspect of the decision below (Pet. 5).

CONCLUSION

The decision below is in accord with the decisions in other circuits and is not in conflict with applicable decisions of this Court. It is respectfully submitted that the petition should be denied.

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OCTOBER 1942.

APPENDIX

Revenue Act of 1932, c. 209, 47 Stat. 169:

SEC. 501. IMPOSITION OF TAX.

(a) For the calendar year 1932 and each calendar year thereafter a tax, computed as provided in section 502, shall be imposed upon the transfer during such calendar year by any individual, resident or nonresident, of property by gift.

(b) The tax shall apply whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property is real or personal, tangible or intangible: * * *

* * * * * *

SEC. 506. GIFTS MADE IN PROPERTY.

If the gift is made in property, the value thereof at the date of the gift shall be considered the amount of the gift.

Treasury Regulations 79 (1936 ed.):

ART. 2. *Transfers reached.*—The statute imposes a tax whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property is real or personal, tangible or intangible. Thus, for example, a taxable transfer may be effected by the declaration of a trust, * * *. Inasmuch as the tax also applies to gifts indirectly made, all transactions whereby property or property rights or interests are donatively passed or conferred upon another, regardless of the means or device employed, constitute gifts subject to tax.

ART. 3. [as amended by T. D. 5010, 1940-2 Cum. Bull. 293]. *Cessation of donor's dominion and control.*—The tax is not imposed upon the receipt of the property by the donee, nor is it necessarily

determined by the measure of enrichment resulting to the donee from the transfer, nor is it conditioned upon ability to identify the donee at the time of the transfer. On the contrary, the tax is a primary and personal liability of the donor, is an excise upon his act of making the transfer, is measured by the value of the property passing from the donor, and attaches regardless of the fact that the identity of the donee may not then be known or ascertainable.

As to any property, or part thereof or interest therein, of which the donor has so parted with dominion and control as to leave in him no power to change the disposition thereof, whether for his own benefit or for the benefit of another, the gift is complete. * * *.

* * * * *

ART. 17. *Gifts made in property.*—A gift made in property is subject to the tax in the same manner as a gift of cash, and the amount of the gift is the value of the property at the date of the gift.

* * * * *

ART. 19. *Valuation of property.*—(1) General.—The statute provides that if the gift is made in property, the value thereof at the date of the gift shall be considered the amount of the gift. * * *.

* * * * *

(7) *Annuities, life, remainder, and reversionary interests.*—For valuation of annuities purchased from life insurance companies or other companies issuing annuity contracts, see subdivision (9) of this article. In case the donor creates a trust under which a specified annuity is payable to the donee, the value of such gift should be determined by using Table A or Table B, whichever is applicable, shown at the end of this article. * * *

* * * * *

If an annuity is to be paid during the life of an individual and in any event for a definite number

of years, or for more than one life, or in any other manner rendering inapplicable both Table A and Table B, the case may be stated to the Commissioner, who will thereupon make the computation and advise the donor thereof. In making such calculations when life interests or remainders upon life interests are involved, use will be made of the Actuaries' or Combined Experience Table of Mortality, as extended (that being the basis of Table A), with interest at 4 percent per annum compounded annually.

If a gift consists of the donor's right to receive the entire income of certain property during the life of Z, or for a term of years, and the annual rate of income for a period equal to or exceeding the life expectancy of Z, or for such term of years, is fixed or definitely determinable at the time of the gift, then the value of the gift should be computed as explained above in the case of an annuity. If the rate of annual income is not determinable, or if the donor is entitled merely to the use of non-income-producing property, a hypothetical annuity at the rate of 4 percent of the value of the property should be made the basis of the calculation.

If the gift is of a remainder or reversionary interest subject to an outstanding life estate, the value of the gift will be obtained by multiplying the value of the property at the date of the gift by the figure in column 3 of Table A opposite the number of years nearest to the age of the life tenant. In case the remainder or reversion is subject to an estate for a term of years, Table B should be used.

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U. S. GOVERNMENT PRINTING OFFICE: 1942

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JAN 9 1943

No. 429

In the Supreme Court of the United States

OCTOBER TERM, 1942

HURLBUT W. SMITH, PETITIONER

v.

FRANK J. SHAUGHNESSY, COLLECTOR OF INTERNAL REVENUE OF THE UNITED STATES FOR THE TWENTY-FIRST DISTRICT OF NEW YORK

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT